

ECONOMIC REFORM THROUGH POLITICAL LEADERSHIP  
IN CHINA'S STATE-OWNED ECONOMY

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# ECONOMIC REFORM THROUGH POLITICAL LEADERSHIP IN CHINA'S STATE-OWNED ECONOMY

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This dissertation examines the impact of political leadership on economic reform in China's state-owned economy. I argue that the heads of public sector organizations, at the central level and below, shape reform policy experimentation and implementation through their choices concerning organizational strategy and structure. Following a review of the key state-owned enterprise reform policies in China since 1978, I utilize case study analysis to assess the effects of political leadership exercised by consecutive chairmen of a central state-owned enterprise on the firm's reform. As the government-directed restructuring of state-owned assets remains an important component of economic reform in China, I next use logistic regression models to analyze the effects of political leadership on mergers among central state-owned enterprises between 2003 and 2015. Finally, I identify four mechanisms that link the organizational change fashioned by political leadership with broader evolution in the institution of state ownership.

## BIOGRAPHICAL SKETCH

Wendy Leutert is from Bradford, Pennsylvania and Naples, Florida. She attended Wellesley College, graduating *summa cum laude* with honors in both political science and philosophy. After studying Mandarin at Cornell University's Full-year Asian Language Concentration (FALCON) Program and at U.C. Berkeley's Inter-University Program for Chinese Language Studies (IUP), she earned a master's degree in international relations (Mandarin-taught program) from Tsinghua University and worked for International Crisis Group in Beijing. She received her master's degree in government from Cornell University in 2014 and her Ph.D. in 2017. She is fluent in Mandarin Chinese.

This dissertation is dedicated to my family and to my teachers.

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## Introduction

### **Economic Reform through Political Leadership**

China Building Company, a central state-owned enterprise in the construction industry, celebrated its first decade of operations in the twenty-first century with a milestone: the number and value of its contracts for projects overseas surpassed that for projects within China. This marked a new era for an enterprise that originated in the Communist Party of China (CCP)'s efforts to advance national industrialization during the 1950s. For decades, China Building Company focused on domestic development through its nationwide network of engineering bureaus. Its earliest commercial forays into international markets were highly centralized, reflecting its roots in a planned economy. Its headquarters dispatched delegations to foreign governments to cultivate relationships for potential projects in an approach that company leaders termed “point to point” (点对点, *dian dui dian*) or “direct line style” (直线式). Later, China Building Company also began to bid for international tenders through a tightly centralized internal process. It referred to overseas projects by number, just as it had for domestic projects during the planned economy period.

By the early 2010s, changes in the company's behavior and organizational structure had become evident to its clients—governments and developers in now more than 50 countries in Central Asia, Africa, Latin America, and Europe. China Building Company's engineering bureaus, which were responsible for carrying out the actual construction work, began to approach them to discuss potential projects, particularly small projects for which they now could exercise bidding and management authority

and sign their own contracts. Yet in 2016, another shift occurred. China Building Company headquarters revoked the engineering bureaus' authority to independently authorize and manage small project contracts. It recentralized administrative authority by establishing a new subsidiary responsible for all international business and even suggested the dispatch of engineering teams from Beijing to tour client countries and recommend possible infrastructure projects. In less than a decade, China Building Company's overseas expansion efforts transformed from centralized to decentralized and back again. At the same time, corresponding shifts in influence occurred between its administrative-oriented headquarters, more market-oriented engineering bureaus, and other entities within the firm.

China's "economic reform" writ large is invoked to explain such a wide variety of political, economic, and social phenomena that micro-level changes at the organization level receive little critical attention. What explains changes in the economic reform of state-owned enterprises in China—both over time and across units? An organization-level analysis reveals that the process of economic reform does not exhibit linear trends of decentralization or consolidation of authority and assets. For state-owned enterprises like China Building Company, this is manifest in changes in the levels of marketization of global expansion efforts, shifts in influence among market-oriented and administrative entities within the firm, and how intra-firm entities conceptualize their relationship with international markets. For the central government's portfolio of state-owned enterprises as a whole, economic reform can be broadly conceptualized as a dual process involving government-directed restructuring of state-owned assets as well as the extension of decision-making authority away from

the state toward markets. Organization-level analysis here too reveals significant variation. For example, between August 2003 and May 2017, 88 out of 189 central state-owned enterprises underwent mergers or other forms of major restructuring.

Organizational change at the enterprise level is linked with broader changes in the institution of state ownership in China. Since the 1978 advent of Chinese market reforms, several important shifts in the institution of state ownership have occurred. State ownership has expanded to include state ownership and control of capital as well as of assets. It is now concentrated in a group of large state-owned enterprises in sectors that the Chinese government has designated as strategically important, even as the overall proportion of state ownership in the economy has declined. In addition, the state has steadily devolved both ownership and control rights to enterprises and their managers as well as non-state shareholders—state ownership and control is no longer absolute. Finally, the orientation of state ownership toward an internationalizing domestic economy has expanded to include the participation of state-owned enterprises in international capital markets and their ownership and control of assets and capital overseas. What factors explain these changes in the institution of state ownership in China?

### ***Competing Perspectives***

I argue that political leadership at the organization level is the omitted factor in existing research on China's economic reform. While scholars look at China from myriad angles, they neglect one of the most important—elite agency spanning the apex of the political system and the grassroots. Yet the political leadership exercised

by the heads of public sector organizations at multiple levels and across functional domains is a crucial part of what constitutes the “authority” in “authoritarianism” in China. The under-theorized factor of political leadership helps to explain changes in economic reform within and across state-owned enterprises as well as changes in the institution of state ownership. The heads of organizations bring about change by determining the specific strategies through which to achieve broad central goals and by altering organizational structure. Organizational change fashioned by political leadership can also generate broader institutional change through multiple channels, such as the political promotion of successful organizational leaders, the center’s designation of a particular organization as a model for emulation, and formal and informal sharing of organizations’ reform experiences. Studying political leadership at the organization level provides analytical leverage needed to answer three key questions in the study of Chinese and comparative politics: 1.) what factors affect policy experimentation and implementation? 2.) why do the structure and behavior of political and economic organizations change over time? and 3.) how are these organizational changes linked to broader institutional change?

Existing research has largely failed to move from studying Chinese leaders to examining their actual exercise of political leadership and its impact on organizations and institutions.<sup>1</sup> I argue that extending the concept of political leadership beyond the top national leaders to the heads of central-level government agencies, state-owned enterprises, and subnational governments is essential to understand economic reform

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<sup>1</sup> Notable exceptions are Jean-Luc Domenach, *The Origins of the Great Leap Forward: The Case of One Chinese Province* (Westview Press, 1995); John A. Donaldson, “Why Do Similar Areas Adopt Different Developmental Strategies? A Study of Two Puzzling Chinese Provinces,” *Journal of Contemporary China* 60 (2009): 421-444.

in contemporary China. Neither central directives nor external market forces can fully explain organizational and institutional change. Furthermore, the decentralization of decision-making authority away from the central planners has increased the space for political leadership at the organization level. In a planned economy, the center determines national development priorities, the allocation of resources to different industries and regions, the management of individual enterprises (for example, their inputs, production, sales, and investments), the nature of wage systems (for example, wage amounts and wage differentials), and even the assignment of individuals to particular work units.<sup>2</sup> Since the 1978 advent of Chinese economic reform, heads of public sector organizations have gained significant autonomy to shape policy experimentation and implementation by determining the specific strategies to achieve broad central objectives, and by altering the structures of the organizations they lead.

Beyond political leadership, current scholarship suggests two alternative perspectives on interlinked processes of organizational and institutional change in China's state-owned economy. A top-down, "strategic design" perspective emphasizes deliberate choices by top national leaders about economic policies, institutions, organizational forms, and resource allocations. In this view, policy experimentation may be linked with elite power struggles, as competing national leaders carry out pilot programs or influence local experimentation and then use the results to support their preferred positions. For example, Hongbin Cai and Daniel Treisman (2006) suggest that central authorities often initiate and even direct what may appear to be local

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<sup>2</sup> Robert Wade, "The Relationship Between Political Leadership and Economic Development in Socialist Countries," *Political Leadership and Economic Development: Korea and China*, ed. Se-Hee Yoo (Seoul: Institute for Sino-Soviet Studies, Hanyang University, 1983): 20.

experiments, arguing that local policy experiments are “gambits in a game played between competing factions centered in Beijing.”<sup>3</sup> Elite politics at the center can also impact the timing of reform policy implementation, as different individuals might propose different timetables for reform, or seek to advance or delay particular reform policies. In addition, a strategic design perspective highlights the institutional mechanisms by which national elites shape the incentives that affect local behavior. For instance, Susan Shirk (1993) details Deng Xiaoping’s strategy of “playing to the provinces” by using fiscal decentralization to local governments to incentivize improved enterprise performance and to build a political constituency supportive of further reforms.<sup>4</sup> Sebastian Heilmann (2008) details the institutional practice of “experimentation under hierarchy,” in which policy-makers at the center selectively integrate local experiences into national policy.<sup>5</sup> Finally, national leaders may attempt to control implementation of reform policies formally through personnel appointments or informally through patron-client relationships connecting central and local officials.<sup>6</sup> For example, Yasheng Huang (2006) argues that Beijing systematically appointed officials with greater experience and ties with the center to govern those provinces with higher levels of international trade and foreign direct investment.<sup>7</sup>

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<sup>3</sup> Hongbin Cai and Daniel Treisman, “Did Government Decentralization Cause China’s Economic Miracle?” *World Politics* 58, no. 4 (2006): 505-535.

<sup>4</sup> Susan L. Shirk, *The Political Logic of Economic Reform in China* (Berkeley, CA: University of California Press, 1993).

<sup>5</sup> Sebastian Heilmann, “From Local Experiments to National Policy: The Origins of China’s Distinctive Policy Process,” *The China Journal*, 59 (2008): 1-30; Sebastian Heilmann, “Policy Experimentation in China’s Economic Rise,” *Studies in Comparative International Development* 43, no. 1 (2008): 1-26.

<sup>6</sup> Pierre F. Landry, *Decentralized Authoritarianism in China* (New York: Cambridge University Press, 2008).

<sup>7</sup> Yasheng Huang, *Selling China: Foreign Direct Investment during the Reform Era* (New York: Cambridge University Press, 2006).

A top-down, “strategic design” perspective on China’s economic reform emphasizes the center’s diverse means of exerting economic and political control, including the power to rework rules related to ownership, enterprise restructuring, market entry and exit, business scope, technology, and service standards.<sup>8</sup> The state exercises both regulative and constitutive authority. It can create new standards and laws, for example through industry-specific regulations. It can also create new categories of organizational forms or determine the “strategic value” of an industry.<sup>9</sup> A strategic design perspective also points to the state’s role as an institutional entrepreneur, for example, in the design of a dual-track economic system combining plan and market during the 1980s, which permitted firms to sell goods produced in excess of central targets at market prices and to retain and allocate the returns. Last but certainly not least, the state maintains political control through the cadre management system, by which the CCP governs cadres at all levels by controlling appointments, evaluations, transfers, and dismissals.

In contrast, a bottom-up “organic transformation” perspective highlights actors’ on-the-ground adaptation to changing external conditions, particularly rising market competition, and their network interactions in the context of economic decentralization.<sup>10</sup> For example, enterprises may adapt to changing environments by adjusting their organizational structures, seeking to forge alliances with other firms, or

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<sup>8</sup> Roselyn Hsueh, *China’s Regulatory State: A New Strategy for Globalization* (Ithaca, NY: Cornell University Press, 2011): 22.

<sup>9</sup> On the concept of strategic value in Chinese industry, see Hsueh 2011 and Roselyn Hsueh, “State Capitalism, Chinese-Style: Strategic Value of Sectors, Sectoral Characteristics, and Globalization,” *Governance* 29 (2016): 85-102.

<sup>10</sup> On the decentralization of China’s economic system, see Chenggang Xu and Juzhong Zhuang. “Why China Grew: The Role of Decentralization,” *Emerging from Communism: Lessons from Russia, China, and Eastern Europe*, eds. Peter Boone, Stanislaw Gomulka, and Richard Layard (Cambridge, MA: MIT Press, 1998): 183-212.

looking for new sources of capital. What may begin as scattered or idiosyncratic incidences of adaptation can become standardized and spread such that existing institutions must ultimately evolve to accommodate them.<sup>11</sup> For example, Victor Nee and Sonja Opper (2012) argue that capitalism in China emerged “from below” as entrepreneurs in the Yangtze River Delta built networks that generated and enforced business norms and facilitated financing for fledgling private firms, ultimately diffusing market institutions nationwide.<sup>12</sup> As Katherine Verdery (2003) describes such bottom-up adaptation in a post-socialist context: “Daily life rested on constant improvisation, generating routines and networks that could at length produce their own social infrastructure, which would then shape outcomes at the top at least as much as the other way around.”<sup>13</sup>

A bottom-up “organic transformation” perspective also underscores the numerous ways in which local agents seek to deliberately manipulate existing conditions to their advantage. For example, Joseph Fewsmith and Xiang Gao (2014) argue that local officials’ lack of accountability to constituents and profit orientation—institutional byproducts of the cadre management system and fiscal decentralization—enables some county leaders to collect rents and enhance their influence at the expense of central dictates.<sup>14</sup> Other officials exploit the information asymmetries inherent in the decentralized and fragmented nature of China’s political system in order to

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<sup>11</sup> Kellee S. Tsai, “Adaptive Informal Institutions and Endogenous Institutional Change in China,” *World Politics* 59, no. 1 (2006): 116-141.

<sup>12</sup> Victor Nee and Sonja Opper, *Capitalism From Below: Markets and Institutional Change in China* (Cambridge, MA: Harvard University Press, 2012).

<sup>13</sup> Katherine Verdery, *The Vanishing Hectare: Property and Value in Postsocialist Transylvania* (Ithaca, NY: Cornell University Press, 2003): 27.

<sup>14</sup> Joseph Fewsmith and Xiang Gao, “Local Governance in China: Incentives and Tensions,” *Daedalus* 143, no. 2 (2014): 170-183.



selectively implement policies that benefit their interests. For instance, Kenneth Lieberthal and Michel Oksenberg (1988) describe how some officials take advantage of the self-contained nature of public sector units in China by publicly declaring their support for policies they oppose but then doing nothing to carry them out within their units.<sup>15</sup> Instead of engaging in “directed improvisation,” in which the center directs and local agents improvise, such instances suggest that actors may on occasion deliberately ignore the center’s directives and simply improvise to suit their own scripts.<sup>16</sup>

Bottom-up, organic transformation accounts of economic reform assume significant decentralization of economic and political authority. Because of this, they typically situate their analyses within center-local analytical frameworks, focus on actors and networks at the local level, and address subnational variations in development outcomes among localities or enterprises. They do acknowledge that the state deliberately designs political institutions, such as the cadre management system, to centralize authority by incentivizing or even directing actors to behave in particular ways. They argue, however, that more important than these top-down controls is the space that decentralization creates for interpretation, experimentation, learning, competition, and cooperation for all actors—from local governments to private enterprises to individuals. Further, organic transformation accounts emphasize that actors’ behavior and the outcomes of the economic reform process may in fact diverge significantly from the center’s original intentions.

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<sup>15</sup> Kenneth Lieberthal and Michel Oksenberg, *Policy Making in China: Leaders, Structures, and Processes* (Princeton, NJ: Princeton University Press, 1988): 166-167.

<sup>16</sup> See Chapter 2, “Directed Improvisation,” Yuen Yuen Ang, *How China Escaped the Poverty Trap* (Ithaca, NY: Cornell University Press, 2016).

Both top-down and bottom-up approaches fall short in explaining organizational and institutional change during economic reform. National leaders and central-level policies do not control—and in most cases they do not attempt to directly control—the internal decision-making or the specific actions of individual public sector organizations. In practice, the decentralization of political and economic authority and the self-contained nature of these organizations in China can often make it difficult for administrative superiors to even ascertain what is actually occurring within them, let alone to control their behavior. But on the other hand, it would be inaccurate to suggest that economic reform in China is an organic process in which public sector organizations adapt to external changes as they see fit, or that it is a spontaneous product of individuals and organizations interacting freely in a decentralized context. Government intervention and institutional mechanisms for central control, such as the cadre management system, continue to characterize China's political economy. Especially during the early reform era, government bodies routinely intervened in the operations and restructuring of state-owned enterprises, promoted organizational change via government-directed pilots, and sanctioned firms if their behavior deviated from what was considered permissible according to the institution of state ownership at a particular time.

Top-down and bottom-up perspectives also fail to account for changes over time in the institution of state ownership itself. Elite redefinition of the relationship between the state and the economy did shape distinct periods of institutional evolution. That said, a top-down explanation cannot fully explain the micro-level changes that underpinned broader institutional shifts during each of these periods. Similarly,

although the support of national leaders did influence when and which pilot schemes and enterprise reform policies were adopted, they did not control the enterprise responses and market factors that determined both the experimental strategies adopted and their ultimate outcomes. In fact, the proliferation of competing enterprise policies that top leaders advanced at various times actually expanded organization heads' leeway for maneuver. Changing market conditions also influenced shifts in the institution of state ownership in China, for example its reorientation from domestic to international and its expansion to include state-owned capital as well as state-owned assets. Yet neither external conditions nor bottom-up actions can account for other changes, such as the concentration of state ownership in a specific set of industries. Instead, top national leaders at the center continued to shape some of the particular contours of state ownership through a varying mix of administrative interference, direction, and accommodation.

### ***Reform through Political Leadership in China's State-owned Economy***

This project analyzes the impact of political leadership at the organization level on reform in China's state-owned economy. The state sector is the most important area to study economic reform in China today because its share in the domestic as well as the global economy is both large and growing. The contribution of state-owned enterprises to China's industrial output has been estimated at between 25% and 30% in 2014.<sup>17</sup> Moreover, the state's share of the domestic economy is actually increasing: in 2012, state-owned enterprises' share of fixed-asset investments reversed years of

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<sup>17</sup> Nicholas R. Lardy, *Markets Over Mao: The Rise of Private Business in China* (Washington, DC: Peterson Institute for International Economics, 2014).

decline and now is on the rise.<sup>18</sup> The sheer size of China's state-owned economy means that its reform has global implications: if Chinese state-owned companies were a country, they would constitute the world's fourth-largest economy—ahead of Germany, the United Kingdom, France, and India.<sup>19</sup> The growing prominence of China's state firms on the global stage also compels critical attention. Many of its “national champions” are now among the world's largest firms: 48 Chinese central state-owned enterprises appeared on the 2016 Fortune Global 500 list, up from 9 in 1999. They have also expanded rapidly in international markets: central state firms currently operate in 185 countries and regions worldwide, with total overseas assets of \$725.6 billion and 346,000 employees.<sup>20</sup>

With the question of economic reform in China's state-owned economy approached in so many ways, terminological precision is essential. I define economic reform within central state-owned enterprises as an increase in the level of marketization in three areas. The first is the level of marketization of expansion efforts in international markets: is marketization high (when decision-making about resource allocation is decentralized and responds to local market conditions) or low (when decision-making about resource allocation is centralized and seeks to shape local market conditions)? The second is growth in the influence of market-oriented actors relative to administrative actors within the firm. This is measured by the extent to which market-oriented entities can act autonomously of administrative entities. The

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<sup>18</sup> Gavekal Dragonomics, “The State of the State Sector,” March 2017.

<sup>19</sup> “China's State Firms Are Bigger than Germany and That's a Problem,” Bloomberg News, August 31, 2016.

<sup>20</sup> Yunbi Zhang, “Nation Will Fine-Tune SOE [State-owned Enterprise] Management Abroad,” *China Daily*, March 22, 2017.

third is how these intra-firm entities conceptualize their relationship with international markets: do they define their functions through active engagement with international markets or do they view international markets through an administrative lens? I define economic reform across central state-owned enterprises as comprising the government-directed restructuring of state-owned assets (for example, through mergers) and the extension of decision-making authority away from the state toward markets (for example, through corporate governance development or public listing of state-owned assets).

I investigate the impact of political leadership exercised at the organization level on economic reform by examining the heads of central state-owned enterprises and the directors of the State-owned Assets Supervision and Administration Commission (SASAC), China's government ownership agency.<sup>21</sup> In China's state-owned economy, central state-owned enterprises are the largest in terms of assets and revenues, make the most profits, pay the most taxes, and possess the greatest strategic importance. These firms dominate numerous sectors in China's domestic economy—from petroleum to telecommunications to aviation to electricity generation and transmission. Each central state-owned enterprise is typically a multi-layered enterprise group with more than 100 subsidiary entities.<sup>22</sup> Their heads are officials who hold the equivalent of either vice-ministerial or department-level administrative

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<sup>21</sup> The Hu Jintao administration established SASAC in 2003 as a special agency of the State Council, China's main government body. This study focuses on the SASAC at the central level; it does not examine the parallel SASACs established to administer state-owned assets at the subnational levels.

<sup>22</sup> Lisa A. Keister, *Chinese Business Groups: The Structure and Impact of Interfirm Relations During Economic Development* (Oxford: Oxford University Press, 2000).

rank.<sup>23</sup> The directors of SASAC are responsible for the oversight, performance assessment, and reform of the central government's portfolio of state-owned enterprises.

### ***Overview of the Study and Methods***

In Chapter 1, I introduce the political leadership approach to studying economic reform in China. In Chapter 2, I detail key enterprise reform policies since 1978 to document the creation and expansion of space for political leadership at the organization level. Chapter 3 and Chapter 4 assess the impact of political leadership at the organization level on economic reform within and across central state-owned enterprises. In Chapter 3, I use a most-similar case study design to analyze the effects of political leadership by consecutive chairmen of a central state-owned enterprise on firm-level reform outcomes: changes in the levels of marketization of the firm's global expansion strategy, shifts in influence among intra-firm entities, and how they conceptualize their relationship to international markets. The empirical analysis in both Chapter 3 and Chapter 4 evaluates the political leadership explanation against competing explanations derived from the top-down strategic design and bottom-up organic transformation perspectives on economic reform. Finally, Chapter 5 connects the organizational change wrought by political leadership with the broader evolution of the institution of state ownership in China.

The methodological approach of this dissertation exhibits “analytic eclecticism”: pragmatic triangulation of methods and data, creative combination of

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<sup>23</sup> The ranks of these individuals depend on the administrative ranks of their firms.

multiple mechanisms, and investigation of broad, substantive questions grounded in the social and historical circumstances of China's state-owned economy.<sup>24</sup> First, I employ mechanisms-based analysis, using process tracing to study how central state-owned enterprise heads exercise political leadership to shape economic reform at the firm level and use a varied repertoire of tactics to advance their agendas. I also investigate the feedback loops between organizations and institutions and identify several potential mechanisms through which organizational change in China's state-owned economy can generate co-evolution in institutions such as state ownership. This mechanisms-centered mode of analysis disaggregates complex organizations based on internal structures, relationships, and processes; reveals the strategic interactions among organizational and individual actors; and illuminates the institutional and social environments in which they operate.<sup>25</sup> In addition, I use variable-based, large-n analysis to examine the relationship between the political leadership exercised by organizational leaders at multiple levels and the likelihood of mergers for all central state-owned enterprises between 2003 and 2015. This methodological approach makes it possible to identify systematic relationships across a large number of units and to assess their relative strength.

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<sup>24</sup> Rudra Sil and Peter J. Katzenstein, *Beyond Paradigms: Analytic Eclecticism in the Study of World Politics* (New York: Palgrave Macmillan, 2010).

<sup>25</sup> Kevin O'Brien, "Discover, Research (Re)design, and Theory Building," *Doing Fieldwork in China*, eds. Maria Heimer and Stig Thøgersen (Honolulu, HI: University of Hawaii Press, 2006); Elisabeth J. Wood, "Field Methods" in *The Oxford Handbook of Comparative Politics*, vol. 4, eds. Carles Boix and Susan C. Stokes (New York: Oxford University Press, 2007).

## Chapter 1

### **Political Leadership at the Organization Level**

Most scholars of China's politics are well acquainted with top national leaders—such as Deng Xiaoping, Zhu Rongji, Wen Jiabao or Xi Jinping—and their roles in the country's economic reform process. However, fewer are familiar with individuals like Li Rongrong, founding director of government ownership agency the State-owned Assets Supervision and Administration Commission (SASAC), or Chen Qingtai, former head of the Second Motor Vehicle Manufacturing Plant. Researchers have traditionally paid less attention to heads of public sector organizations—government bodies, Party organs, or state-owned enterprises—even at the central level. Instead, many scholars emphasize the institutional constraints shaping China's political economy, from the level of top central leadership down to individual citizens.<sup>26</sup> Embrace of institutional approaches has prompted organization heads to be largely written off as bureaucrats with little autonomy engaged primarily in management or administrative tasks. In contrast, this chapter argues that organization heads need to be taken seriously as political leaders deeply and directly engaged in the process of economic reform. I propose a political leadership approach to studying economic reform that proceeds in four parts. It highlights organization heads' bounded autonomy to make choices within organizational and institutional constraints,

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<sup>26</sup> Victor Nee and David Stark, *Remaking the Economic Institutions of Socialism: China and Eastern Europe* (Palo Alto, CA: Stanford University Press, 1989); Jean C. Oi, *Rural China Takes Off: Institutional Foundations of Economic Reform* (Berkeley, CA: University of California Press, 1999); Susan L. Shirk, *The Political Logic of Economic Reform in China* (Berkeley, CA: University of California Press, 1993); Samantha A. Vortherms, "Between the Center and the People: Localized Citizenship in China," (Ph.D. dissertation, University of Wisconsin-Madison, 2017).



identifies the main methods through which they actually exercise political leadership, discusses the role of political leadership in policy experimentation and implementation processes, and analyzes the obstacles to a political leadership approach.

I define political leadership at the organization level as a process of influence through which the heads of public sector organizations seek to maintain continuity or to bring about change in the structure and operations of their organizations and others' behavior that would not have otherwise occurred.<sup>27</sup> This study focuses specifically on those individuals at the helm of central-level state-owned enterprises and government bodies in China's state-owned economy.<sup>28</sup> Studying political leadership at the organization level involves closely analyzing the top-ranked individual in a given organization and the effects of their choices and actions on the structure and behavior of that organization and those under its immediate administrative authority.<sup>29</sup> What are the strategies that organizational leaders advance to achieve central reform goals or to maintain the status quo? How do they alter or maintain the structures of the organizations that they lead? Locating the study of political leadership at the organization level enables fine-grained analysis of the factors that condition political leadership, the methods through which it is exercised, and its organizational and

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<sup>27</sup> This study centers on the realm of formal politics, in which officials hold positions of formal authority as the heads of government bodies, Party organs, and state-owned enterprises at multiple levels of government.

<sup>28</sup> Public sector organizations in China also include a wider array of entities, such as schools and hospitals at multiple levels of government; however, these organizations are beyond the scope of this study.

<sup>29</sup> This study focuses on individual heads of organizations, rather than broader leadership groups (领导班子, *lingdao banzi*), because top leaders typically exercise predominant influence and ultimate decision-making authority in political and economic organizations in China. Similarly, although organizational leaders may be active in broader networks of political elites, because this study addresses organization level outcomes, I focus on top leaders' individual exercise of political leadership within the organizations that they lead and its impact at the organization level.

institutional impact. A political leadership approach entails empirically evaluating this impact relative to the effects of other factors.<sup>30</sup>

I use the term *political* leadership to emphasize that public organization heads in China are first and foremost political rather than administrative actors. Scholarship on public administration has collapsed the crisp Weberian distinction between professional politicians and professional bureaucrats, showing how civil servants can exercise leadership within administrative organizations by making decisions, acting strategically, leveraging technical expertise to influence others, and imbuing the work of bureaucracies with values.<sup>31</sup> The central-level organization heads examined in this study are more politicians than bureaucrats in fact as well as function. Leaders of public sector organizations in China are Party politicians as well as state bureaucrats. Most of them do not expect—nor do they desire—lifetime careers in a particular public sector organization, even if they may spend years working there. Instead, these leading cadres expect that the Party center will regularly transfer them to different geographic locations and/or functional areas of the Chinese government or Party bureaucracy, either via new appointments or cadre exchanges, and most of them strive for promotion to higher-ranked central-level positions.<sup>32</sup> Individual political gain—

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<sup>30</sup> These may include factors external to the organization, such as a major policy shift or change in external market conditions.

<sup>31</sup> On Weber's original distinction between professional politicians and professional bureaucrats and a comparative study of the empirical overlap between the two, see Max Weber, "Politics as a Vocation" in *From Max Weber: Essays in Sociology*, eds. and trans. H. H. Gerth and C. Wright Mills (New York: Routledge, 2009 [1947]): 77-128. See also Joel D. Aberbach, Robert D. Putnam, and Bert A. Rockman, *Bureaucrats and Politicians in Western Democracies* (Cambridge, MA: Harvard University Press, 1981). For an overview of the literature on administrative leadership, see Montgomery Van Wart, "Administrative Leadership Theory: A Reassessment After 10 Years," *Public Administration* 91, no. 3 (2013): 521-543.

<sup>32</sup> The CCP institution of cadre exchange (干部交流制度, *ganbu jiaoliu zhidu*) is the routine rotation of Party and state officials to serve in different posts and/or in different localities across the country. Its

beyond the context of a particular organization—is equally if not more important to organization heads in China than simply gaining resources and authority for their particular organizations. As a senior executive of a Chinese central state-owned enterprise put it bluntly: “State-owned enterprise leaders will always think more about their own promotion (升官, *shengguan*) than about the particular interests of their enterprises.”<sup>33</sup>

A political leadership approach links three levels of analysis: individual, organizational, and institutional. It integrates analysis of the institutional factors that mediate influence—the general form of the state and economy within which elite groups operate—with attention to how members of those groups exercise this influence relative to others through their decisions and actions.<sup>34</sup> Scholarship addressing the scope for agency relative to institutional constraints has focused primarily on collective actors—like interest groups, organizations, networks, and advocacy coalitions—rather than individual actors.<sup>35</sup> In contrast, a political leadership approach contends that individual actors can also be a source of endogenous institutional change. Specifically, it highlights organizational leaders’ capacity to make choices within constraints and to engage in strategic action. These individual actors play key roles in the interactions between endogenous and exogenous sources of institutional change—such as critical junctures and external shocks—and the

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aims include: promoting organizational learning, evaluating cadre performance for potential further promotions, spreading successful policies, and limiting localism and corruption.

<sup>33</sup> Interview with senior executive of central state-owned enterprise, Beijing, October 2015. All interviews cited in this study followed the protocol approved by the Cornell Institutional Review Board, number: 1507005681.

<sup>34</sup> Anthony Giddens, *The Class Structure of the Advanced Societies* (London: Hutchinson, 1973).

<sup>35</sup> Jan Olsson, *Subversion in Institutional Change and Stability: A Neglected Mechanism* (London: Palgrave Macmillan, 2016): 4.

political processes of influence, competition, and conflict that they involve.<sup>36</sup> A political leadership approach also illuminates the everyday politics of institutional change by showing how organizational leaders exercise influence relative to superiors and subordinates in specific issue areas. Organizationally grounded analysis suggests the limitations of viewing institutional change as the product of abstract, unconstrained clashes between a dichotomous set of “actors that support and defend institutional rules, norms, and practices and opponents who question and try to undermine institutions.”<sup>37</sup>

A political leadership approach to the study of economic reform has four key characteristics. First, it foregrounds individual actors and the concept of choice within institutional and organizational constraints. To use Douglass North (1990)’s classic analogy, if institutions are the “rules of the game” and organizations are the “players of the game,” then organization heads make choices about how organizations will actually play the game, either in accordance with existing rules or challenging their limits.<sup>38</sup> Organization heads also make choices that shape organizational structure as well as behavior. For example, they make decisions about organizational form and purpose within “organizational repertoires”: the set of alternative organizational forms

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<sup>36</sup> Critical junctures are limited periods of time in which the range of plausible choices and scope for policy action expands and the potential consequences of actions are greater. Giovanni Capoccia and R. Daniel Kelemen, “The Study of Critical Junctures: Theory, Narrative, and Counterfactuals in Historical Institutionalism,” *World Politics* 59, no. 3 (2007): 343.

<sup>37</sup> Olsson 2016: 5.

<sup>38</sup> Douglass C. North, *Institutions, Institutional Change and Economic Performance* (New York: Cambridge University Press, 1990): 4-5. As Olsson 2016 observes: “the rule of the game metaphor seduces us to accept the view of a clear distinction between the rules of the game and the game actually played, as if the game in itself is not allowed to interact with its rules.” Olsson 2016: 14.

available to actors in a given institutional context.<sup>39</sup> In addition, a political leadership approach highlights the hierarchies of influence that exist among actors themselves, for example between an organizational leader and his subordinates. Organizations and institutions do not constrain all actors uniformly: some actors may have greater ability than others to maintain or to modify existing organizations and institutions. Finally, a political leadership approach at the organization level enables study of fine-grained organizational and institutional change in the short- to medium-term (over a period of several years to several decades) by locating its analysis at the micro-level.

Studying political leadership at the organization level calls for rethinking some conventional assumptions about the roles that heads of public sector organizations play in Chinese politics. Scholars rarely use the term “political leadership” to describe the activities of officials below or even at the ministerial level. Instead, they often portray heads of central ministries or state-owned enterprises as bureaucrats performing primarily managerial and administrative functions. The conventional wisdom remains that top officials and advisors at the center make decisions; public sector organizations and their heads carry them out. Such a division reflects Craig Hickman’s (1990) stylized portrayal of leadership and management as two opposite ends of a continuum: leaders engage in experimental, visionary, flexible and creative activities, while managers carry out more structured, controlled, deliberate, and orderly activities.<sup>40</sup>

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<sup>39</sup> Organizational repertoires may change exogenously (for example through changes in legal categories) or endogenously (for example through organizational innovation). Elisabeth S. Clemens, “Organizational Repertoires and Institutional Change: Women’s Groups and the Transformation of U.S. Politics, 1890-1920,” *American Journal of Sociology* 98, no. 4 (1993): 755-798.

<sup>40</sup> Craig Hickman, *Mind of a Manager, Soul of a Leader* (Austin, TX: University of Texas Press, 1990).

However, the heads of government bodies, Party organs, and state-owned enterprises at the central level and below in China also carry out leadership functions: engaging in experimentation, formulating strategies, restructuring their organizations, adjudicating conflict and taking stands, and requiring, persuading, or coercing others to follow the directions that they set.<sup>41</sup> Bureaucracy and leadership are deeply intertwined, not diametrically opposed, because the operations of public sector organizations in China rarely involve the simple application of authority from the top down. As James M. Burns (1978) writes: “To the extent that it [bureaucracy] exemplifies conflict, power, values, and change in accordance with leader-follower needs, it embodies leadership.”<sup>42</sup> Recognizing that political authority remains highly centralized in China and that organization heads do engage in managerial and administrative work should not preclude taking them seriously as political leaders who possess significant if bounded autonomy and influence in Chinese politics.

A political leadership approach to studying China’s economic reform expands empirical domains of study and offers a new explanation for variation in organizational behavior and structure during economic reform. Opening up the black box of organizations as diverse as central ministries, state-owned enterprises, regulatory agencies, and local environmental protection bureaus is valuable because it provides insight into the functioning of China’s political and economic system. For example, instead of simply comparing lists of experimental pilot programs with

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<sup>41</sup> On leadership functions, see W. Andy Knight, “Distinguishing and Unifying Visionary Leadership and Mechanical Management,” *The Ashgate Research Companion to Political Leadership*, eds. Joseph Masciulli, Mikhail A. Molchanov, and W. Andy Knight (New York: Ashgate Publishing, 2009): 136-137.

<sup>42</sup> James MacGregor Burns, *Leadership* (New York: Harper & Row, 1978): 298.

subsequent central regulations and laws, or promulgated central policies with later implementation outcomes, studying political leadership at the organization level can illuminate how processes of policy experimentation and implementation actually occur. It can help to explain observed variation in the structure and behavior of multiple organizations as well as changes over time within a single organization.

### ***Political Leadership at the Organization Level in China***

The heads of state-owned enterprises and government and Party organizations in China are officials governed by the Communist Party of China (CCP)'s cadre management system.<sup>43</sup> The Party center has long used the cadre management system as an institutional mechanism to control and integrate the governance of localities as well the largest state-owned enterprises.<sup>44</sup> In theory, the Party's authority to appoint, assess, transfer, promote, and remove top officials aligns their individual career incentives with the Party center's objectives.<sup>45</sup> The official cadre evaluation framework has five elements: morality, ability, diligence, performance, and

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<sup>43</sup> At the central level, the fifth department (五局, *wu ju*) of the Central Organization Department's Enterprise Cadre Bureau (企业干部局, *qiye ganbu ju*) directly manages the top leaders of central state-owned enterprises designated as 'important backbone enterprises' in conjunction with higher Party authorities; SASAC appoints top leaders for the remaining central state-owned enterprises in coordination with the Central Organization Department.

<sup>44</sup> On the cadre management system functioning as an institution of central control over local governance, see Pierre F. Landry, *Decentralized Authoritarianism in China* (New York: Cambridge University Press, 2008); Yasheng Huang, *Selling China: Foreign Direct Investment during the Reform Era* (New York: Cambridge University Press, 2006). On the cadre management system functioning to integrate the largest state-owned enterprises with a Party-led system of governance, see Kjeld Erik Brødsgaard, "Politics and Business Group Formation in China: The Party in Control?" *The China Quarterly* 211 (2012): 624-648; Chen Li, "Holding 'China Inc.' Together: The CCP and the Rise of China's *Yangqi*," *The China Quarterly* 228 (2016): 927-949.

<sup>45</sup> Two other important mechanisms of Party control over personnel are staff and budget allotments (编制, *bianzhi*) and the routine circulation of officials to serve in different posts and/or different localities through the institution of cadre rotation (干部交流制度, *ganbu jiaoliu zhidu*).

uprightness (德、能、勤、绩、廉, *de, neng, qin, ji, lian*). Its aim is to incentivize, guide, and homogenize the behavior of Chinese officials by making clear the shared standards by which individuals in disparate posts and localities are assessed. The cadre management system represents the “rules of the game” for participants in the CCP’s internal labor market.

In the context of the cadre management system, Chinese officials’ exercise of political leadership has two main aims. The first is to deliver the goals that the center tasks their organizations to achieve. Economic performance is typically the most important: a large body of scholarship on Chinese officials’ political mobility provides evidence linking economic growth with increased likelihood of promotion.<sup>46</sup> Other studies document officials’ systematic falsification of economic statistics, demonstrating the great lengths to which cadres will go to show that their performance meets central targets.<sup>47</sup> In the cutthroat tournament competition among Chinese officials, each individual has often only several years in which to deliver better results than his peers, in order to be promoted.<sup>48</sup> Political leadership in this economic

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<sup>46</sup> Ye Chen, Hongbin Li, and Li-an Zhou, “Relative Performance Evaluation and the Turnover of Provincial Leaders in China,” *Economics Letters* 88, no. 3 (2005): 421-25; Hongbin Li and Li-An Zhou, “Political Turnover and Economic Performance: The Incentive Role of Personnel Control in China,” *Journal of Public Economics* 89 (2005), 1743–62; Frederick Teiwes, “Normal Politics with Chinese Characteristics,” *The China Journal* 45 (2001): 69-82. Others argue that political connectedness and patronage relationships (assessed by measures such as central government work experience, factional ties, or central appointments for officials at lower levels of government) make promotion more likely. See Jay Chih-Jou Chen, “Elite Mobility in Post-Reform Rural China,” *Issues and Studies* 42 no. 2 (2006): 53-83; Pierre F. Landry, “The Political Management of Mayors in Post-Deng China,” *Copenhagen Journal of Asian Studies* 17 (2005), 31-58; Victor Shih, Christopher Adolph, and Mingxing Liu, “Getting Ahead in the Communist Party: Explaining the Advancement of Central Committee Members in China,” *American Political Science Review* 106, no. 1 (2012): 166-187.

<sup>47</sup> Jeremy L. Wallace, “Juking the Stats? Authoritarian Information Problems in China,” *British Journal of Political Science* 46, no. 1 (2016): 11-29.

<sup>48</sup> For example, Li and Zhou 2005 find that the average tenure for Chinese provincial leaders between 1979 and 1995 is only 3.03 years, while Eaton and Kostka 2014 find that the average tenure for municipal Party secretaries between 1993 and 2011 is 3.8 years. Hongbin Li and Li-An Zhou, “Political



selection environment is essentially an exercise in creative problem solving. How can one achieve the center's goals given the constraints and resources available in a particular organizational setting?

The second impetus for organizational leaders in China to exercise political leadership is what I term "political product differentiation."<sup>49</sup> Officials want to stand out relative to both their peers in similar organizations and their predecessors in a particular post. The best way to be promoted is not just to deliver successful results—it is also to associate oneself indelibly with them. The distinctive strategies that heads of organizations propose and their efforts to alter existing organizational structures thus represent political product differentiation as well as problem-solving efforts to deliver performance gains. Political leadership is an important way by which officials distinguish themselves within the cadre management system and thereby gain competitive advantage. In short, it is a means of individual-level "niche creation" in a political selection environment.

However, not all heads of public sector organizations in China are compliant reformists jockeying for higher-ranked political positions by striving to achieve the center's goals. Some organization heads are content to simply stay in their current positions as long as possible, even up until retirement. Those who assumed leadership

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Turnover and Economic Performance: The Incentive Role of Personnel Control in China," *Journal of Public Economics* 89, no. 9 (2005): 1,753; Sarah Eaton and Genia Kostka, "Authoritarian Environmentalism Undermined? Local Leaders' Time Horizons and Environmental Policy Implementation in China," *The China Quarterly* 218 (2014): 362. On tournament competition in Chinese political economy, see Li-an Zhou, "Governing China's Local Officials: An Analysis of Promotion Tournament Model," *Economic Research Journal* 7 (2007): 36-50.

<sup>49</sup> There are multiple reasons why scholarship on Chinese politics has not yet investigated this motivation for official behavior: the still pervasive idea that heads of state-owned enterprises and sub-national governments act more as bureaucrats than as politicians; the dearth of in-depth studies on individual organizational leaders below the central level; and the implicit assumption of quantitative studies that officials are interchangeable observations differentiated only by demographic attributes.

positions after years or even decades in their organizations often possess deep professional and personal networks and specialized expertise that cannot be exported elsewhere easily. They may perceive that the advantages of staying in their current positions outweigh the risk, uncertainty, and greater pressure of a new organizational environment, despite the potential for greater material and political benefits. Others, eager to move on from their current posts and aware that their tenures may be limited, endeavor to achieve some central goals (like economic growth) while superficially implementing or even ignoring others (like environmental issues).<sup>50</sup> Both those seeking to stay in their current positions and those attempting to move on may choose to ignore or to delay carrying out the center's goals. This is especially likely if central goals are unclear, cannot be easily measured, or if their implementation will negatively impact other actors in an official's organization or locality. Some individuals may even abuse the state authority vested in their positions to advance central goals while simultaneously enriching their organizations—and themselves—in the process.<sup>51</sup>

### ***Bounded Autonomy and Domains of Influence***

“Bounded autonomy” is the autonomous capacity for choice and action within specific organizational and institutional contexts. Institutional and organizational settings do

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<sup>50</sup> Sarah Eaton and Genia Kostka, “Authoritarian Environmentalism Undermined? Local Leaders’ Time Horizons and Environmental Policy Implementation in China,” *The China Quarterly* 218 (2014): 359-380.

<sup>51</sup> A well-known example is Liu Zhijun (刘志军), the former head of the now-abolished Ministry of Railways. During his tenure as minister between 2003 and 2011, Liu oversaw the rapid expansion of China's railway system, in particular its successful development of high-speed rail. However, Liu was convicted in 2013 of corruption and abusing state power.

not determine actors' choices and behavior, even if they constrain and guide it in significant ways. Existing research has primarily examined bounded autonomy as it characterizes state-society or center-local relations.<sup>52</sup> In contrast, this study examines bounded autonomy as it enables heads of public sector organizations to exercise political leadership within particular organizational and institutional contexts. This is expressed by the Chinese term “operational space” (操作空间, *caozuo kongjian*), which refers to the delineated domain within which one possesses freedom of choice and action. In this project, I analyze the sources of bounded autonomy, its limits, and the potential it creates for heads of organizations to exercise political leadership and thereby shape policy experimentation and implementation.

The bounded autonomy of organization heads in China originates from both institutional and organizational sources. Its first institutional source is the cadre management system. While the cadre management system strongly influences organizational leaders' behavior, it is ultimately a mechanism of macro-level control. It incentivizes their efforts to achieve central goals through a combination of carrots (political promotion) and sticks (sanctions). However, it neither specifies nor determines their micro-level choices as they engage in policy experimentation and implementation or political product differentiation. This built-in institutional ambiguity is an important source of autonomy for organizational leaders. Moreover, the cadre management system does not always serve its intended control functions.

Mandatory retirement ages linked with positions of different administrative ranks may

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<sup>52</sup> Andrew Cooper, “State Power and Patterns of Late Development: A Comment on Zhao and Hall,” *Sociology* 28, no. 2 (1994): 539-546; Ding-xin Zhao and John A. Hall, “State Power and Patterns of Late Development: Resolving the Crisis of the Sociology of Development,” *Sociology* 28, no. 1 (1994): 211-229.

prompt officials to seek quick returns through risky or unnecessary investments in order to get promoted.<sup>53</sup> Conversely, they may foster inaction or even illicit behavior if officials infer that due to their ages their current position is likely to be their last. Some even question whether the prospect of promotion is really the primary driver of official behavior to begin with, instead suggesting that the immediate material benefits conferred by a present position may be more desirable than potential future gains in a higher-ranked political position.<sup>54</sup>

Beyond the cadre management system, multiple other institutional factors grant heads of organizations in China bounded autonomy for choice and action during economic reform. The first is the decentralized context in which China's economic reform has occurred. A high degree of decentralization characterizes China's economic system, particularly the relationship between the center and lower levels of government.<sup>55</sup> This decentralization has expanded from authority sharing (分权, *fenquan*), such as localities' participation in decisions about economic planning and distribution of materials during the Mao Zedong era, to the devolution of authority (放权, *fangquan*) for economic decision-making, like that Deng Xiaoping granted to

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<sup>53</sup> In China this is colloquially referred to as the "59 phenomenon" (59 现象, 59 *xianxiang*) or "58 phenomenon" (58 现象, 58 *xianxiang*). On concerns about this issue, see SASAC (Research Office):

《探索与研究：国有资产监督管理和国有企业改革研究报告》 [Exploration and Research: State-Owned Assets Supervision and Management and State-Owned Enterprise Reform Research Report] (Beijing: Jingji chubanshe, 2012): 351.

<sup>54</sup> Yuen Yuen Ang, *How China Escaped the Poverty Trap* (Ithaca, NY: Cornell University Press, 2016): 117.

<sup>55</sup> China has five levels of government: center, province, prefecture, county, and township. Compared to decentralization between the center and the provinces, authority remains more centralized between the provincial and township levels; recentralization has even occurred in some cases. Andrew C. Mertha, "China's 'Soft' Centralization: Shifting *Tiao/Kuai* Authority Relations," *The China Quarterly* 184 (2005): 791-810.

enterprises and localities, especially special economic zones and coastal regions.<sup>56</sup> Decision-making authority is not only decentralized, it is also increasingly fragmented below the central level among a growing number of actors.<sup>57</sup> Heads of the public sector organizations examined here have some if limited scope to engage in “policy entrepreneurship” by framing policy issues and outlining possible alternative approaches to address them.<sup>58</sup> Another factor granting organization heads bounded autonomy for choice and action in their particular organizational realms is the widespread governance practice of “administrative subcontracting” (行政分包, *xingzheng fenbao*). In administrative subcontracting, the center assigns responsibility for carrying out government functions like budget-making or personnel selection and/or public service provision to subordinate organizations or levels of government, which in turn reassign it to those below them, all the way down to the bottom level.<sup>59</sup> A final factor is the nature of central reform objectives themselves. When top authorities in China issue goals for economic reform, they do not specify precisely how these goals are to be achieved. In what Yuen Yuen Ang terms “directed

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<sup>56</sup> Some economic functions of government remain centralized despite this widespread decentralization, such as taxation, banking, and customs.

<sup>57</sup> On fragmented authoritarianism, see: Kjeld Erik Brødsgaard, ed., *Chinese Politics as Fragmented Authoritarianism: Earthquakes, Energy and Environment* (New York: Routledge, 2016); Kenneth Lieberthal and Michel Oksenberg, *Policy Making in China: Leaders, Structures, and Processes* (Princeton, NJ: Princeton University Press, 1988); Andrew C. Mertha, “Fragmented Authoritarianism 2.0: Political Pluralization in the Chinese Policy Process,” *The China Quarterly* 200 (2009): 995-1012.

<sup>58</sup> For example, Xu 2016 details how Liu Zhenya, head of the State Grid Corporation of China, a central state-owned enterprise, engaged in policy entrepreneurship to garner top-level support for controversial ultra-high-voltage transmission networks by framing them as the policy solution to a set of energy and environmental challenges. Yi-chong Xu, *Sinews of Power: Politics of the State Grid Corporation of China* (New York: Oxford University Press, 2016). On policy entrepreneurship, see Andrew C. Mertha, *China's Water Warriors: Citizen Action and Policy Change* (Ithaca, NY: Cornell University Press, 2008); Mertha 2009.

<sup>59</sup> 周黎安 [Zhou Li'an], 《行政发包制》 [Administrative Subcontract], 《社会》 [Society], 34, no. 6 (2014): 1-38; 周黎安 [Zhou Li'an]: 《转型中的地方政府: 官员激励与治理》 [Local Government in Transition: Official Incentives and Governance] (Shanghai: Gezhi chubanshe, 2008).

improvisation,” the center’s reform goals are deliberately broad in scope in order to allow subordinates some leeway to engage in experimentation and figure out how to successfully realize them in accordance with local conditions.<sup>60</sup> Some contend that there may be even greater leeway for subordinates to make divergent and even contradictory interpretations of central goals when conditions of weak institutionalization and fundamental, endemic uncertainty are present.<sup>61</sup>

Organizational leaders’ bounded autonomy also derives from organizational sources. The institutional factors discussed above primarily grant organizational leaders’ scope for bounded autonomy vis-à-vis external actors like administrative superiors. At the same time, their *de jure* (legal) authority as the ‘number-one hands’ (一把手, *yi ba shou*) of their respective organizations widens their scope for choice and action relative to other actors within their particular organizations. Organization heads can draw upon governance and management practices stressing organizational hierarchy, authority, and conformity that trace their origins not only to the communist period but also to Confucian tradition.<sup>62</sup> While clashes among leaders and their subordinates in Chinese organizations do occur, few avenues exist to formally challenge or usurp organization heads’ decision-making authority within the organizations they lead, and those who attempt to do so are likely to face reassignment or dismissal.

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<sup>60</sup> Ang 2016.

<sup>61</sup> For example, Segal 2003 suggests that such conditions during the 1990s enabled local and municipal governments to interpret the concept of ‘people-run [private] enterprise’ (民营企业, *minying qiye*) in widely divergent ways. Adam Segal, *Digital Dragon: High-Technology Enterprises in China* (Ithaca, NY: Cornell University Press, 2003): 39-41.

<sup>62</sup> John Child, *Management in China During the Age of Reform* (Cambridge: Cambridge University Press, 1996).

In practice, administrative hierarchies intersect with functional issue areas and informal networks to delineate organization heads' specific domains of authority. Organization heads exercise influence over restricted ranges of issues, and their authority may be greater with regard to some issues compared with others. For instance, central state-owned enterprise heads have greater leeway for decision-making regarding commercial matters than Party affairs, for which their primary role is to implement the campaigns that the Central Organization Department launches.<sup>63</sup> Decision-making authority within a given issue area also varies by administrative rank. For example, central state-owned enterprise heads possess authority to make decisions about the internal integration of resources within a particular state-owned enterprise group; however, SASAC and the State Council determine which central state-owned enterprises will be merged together, when, and how. Informal networks also shape the contours of organization heads' influence by facilitating their distribution of benefits derived from formal administrative hierarchies to subordinates, especially key allies. By crafting "political settlements"—sustainable balances of relative authority among actors in a particular institutional and organizational context—organization heads can ensure their influence and amplify its reach.<sup>64</sup> In summary, organization heads' domains of authority, within which they possess bounded autonomy to exercise

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<sup>63</sup> Since central state-owned enterprise heads frequently serve as both the chair of the board of directors and the Party secretary, this disparity in influence is not the product of differences in roles between enterprise management and Party positions.

<sup>64</sup> While political settlements are typically studied as distributions of power among elite groups at the national level, their logic can also be applied to examine distributions of influence among sectors or firms at the industry level as well as among actors at the organization level. Mushtaq Khan, "Political Settlements and the Governance of Growth-enhancing Institutions," (2010); Mushtaq Khan, "The Role of Industrial Policy: Lessons from Asia," David Bailey, Keith Cowling, and Philip R. Tomlinson, eds., *New Perspectives on Industrial Policy for a Modern Britain* (Oxford: Oxford University Press, 2015): 79-98.

political leadership, varies by issue area and is a product of both institutional factors as well as administrative hierarchies and informal networks within and among organizations.

### ***Exercising Political Leadership***

Given this bounded autonomy, heads of public sector organizations in China exercise political leadership in multiple ways. They possess primary decision-making authority to appoint key personnel, make major decisions about investments and budgets, determine performance assessment and salary standards for employees, set key priorities for organizational culture and operations, and periodically assess the organization's activities and performance. On a daily basis, heads of organizations exercise political leadership through their authority to review and approve a wide range of detailed organizational matters, from decisions about office relocation to approvals for subordinate leaves and travel. However, while organization heads' exercise of political leadership through these methods shapes day-to-day operations, they are not likely to fundamentally impact reform policy experimentation or implementation in the short- to medium-term.

This study therefore focuses on the two main ways in which heads of organizations exercise political leadership to shape reform policy experimentation and implementation: by determining the specific strategies to respond to central objectives, and by altering organizational structure. These two mechanisms of political leadership are complementary and leaders often use them in tandem. Leaders of the organizations charged with implementing central goals must first interpret them, formulate multiple



possible methods to achieve them, select a strategic path of action (or inaction), determine how to allocate and mobilize organizational resources and personnel, and then endeavor to carry out their preferred strategy. For example, the center tasks central state-owned enterprise heads with realizing the goals of preserving and increasing the value of state assets and building their firms into ‘national champions,’ but state-owned enterprise heads determine how to achieve these goals in their particular organizations. Even within the same organization over time, different leaders may have divergent interpretations of central goals and ideas about how to achieve them, thereby generating variation in the policy experimentation and implementation processes.

Organizational leaders also exercise political leadership by altering the structure of their organizations. Specifically, changes to organizational structure may include: creating, eliminating, or changing existing departments; altering hierarchical authority relationships among subordinate units; and reallocating assets, capital, and personnel within an organization. For example, the “lean and healthy body” (瘦身健体, *shoushen jianti*) reform goal that Premier Li Keqiang announced in May 2016 calls on state-owned enterprise heads to modify their firms’ organizational structures by streamlining layers of management and reducing the number of subsidiaries by at least 20 per cent.<sup>65</sup> State-owned enterprise heads are the ones who will actually decide whether to act in response to this central goal and, if so, specifically how to alter the structure of their organizations in order to achieve it.

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<sup>65</sup> State-owned enterprise heads are responsible for determining which and how many headquarters departments and subsidiaries to eliminate. State Council: 《李克强主持召开国务院常务会议》 [Li Keqiang Chairs State Council Executive Meeting], May 18, 2016.

However, organizational leaders' behavior is not limited only to enacting change. The exercise of political leadership also entails choices about whether to continue predecessors' policies, to not act at all, to delay, to subvert, or even to oppose the implementation of central reform goals. Such choices reflect both leader preferences and strategic assessment about which courses of action (or inaction) are feasible and desirable in a given organizational or institutional setting at a particular time. Take for example the response of many state-owned enterprise heads to efforts by the State Council under Premier Zhao Ziyang's leadership to implement 'tax-for-profit' reform during the 1980s.<sup>66</sup> Many state-owned enterprise heads altered existing economic responsibility systems to make them look like tax-for-profit reforms, while also reclassifying or underreporting their profits in order to protect the proportion of earnings that their enterprises could retain.<sup>67</sup> The nationwide implementation of this reform in 1984 prompted a 22-month decline in industrial state-owned enterprise profits.<sup>68</sup> Focusing solely on the design of institutional arrangements and incentives risks ignoring the broad range of strategic responses to them at the organization level.

While the CCP's personnel management system seeks to motivate organizational leaders to implement central reform objectives, the exercise of political leadership can also have a dark side.<sup>69</sup> Some organizational leaders may personally

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<sup>66</sup> Tax-for-profit reform aimed to legalize enterprises' economic responsibility to the state by substituting an income tax for profit remittance.

<sup>67</sup> Economic responsibility system reforms sought to clarify the rights, interests and responsibilities of state-owned enterprises vis-à-vis the state, through annual one-on-one negotiations with bureaus to establish enterprises' specific targets, profit retention rates, and responsibility for shortfalls or losses.

<sup>68</sup> 章迪诚 [Zhang Dicheng], ed., 《中国国有企业改革编年史, 1978-2005》 [Chronicle of China's State-owned Enterprise Reform] (Beijing: Zhongguo gongren chubanshe, 2006): 110.

<sup>69</sup> Corruption is not a focus of this study. For a recent analysis of corruption in China, see Minxin Pei, *China's Crony Capitalism: The Dynamics of Regime Decay* (Cambridge, MA: Harvard University Press, 2016).

engage in or direct others to carry out rent-seeking and illicit activities such as asset stripping, embezzlement, bribery, or trading political favors. For example, Zhou Yongkang, former head of state-owned enterprise China National Petroleum Corporation (CNPC) and the Ministry of Public Security, was sentenced to life in prison in 2015 for offenses including bribery, abuse of power, and disclosure of state secrets. Jiang Jiemin, the former head of SASAC and associate of Zhou Yongkang at CNPC where he served as general manager and then chairman, was sentenced to 16 years in prison in 2014 for crimes including bribery and abuse of power. The same decentralization of authority that creates space for the exercise of political leadership at the organization level also generates greater leeway for the heads of organizations to engage in illicit activity without effective monitoring and control by administrative superiors.

### ***Moving from Political Leaders to Political Leadership***

Existing research focuses primarily on individual political leaders in China and the relationships among them, not their actual exercise of political leadership at the organization level and its effects.<sup>70</sup> The largest body of scholarship focuses on top national leaders at the apex of the political system. Such works often reconstruct and analyze the dynamics of elite competition and compromise during key historical episodes, such as the Great Leap Forward, the Cultural Revolution, and the Tiananmen

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<sup>70</sup> A notable exception is Wu 2005, who examines the leaders of central-level economic planning agencies in Taiwan to argue that whether a leader was a “strongman” or a “weak chair” determined the degree to which these organs functioned as coordination mechanisms within the Taiwanese economic bureaucracy. Yongping Wu, *A Political Explanation of Economic Growth: State Survival, Bureaucratic Politics, and Private Enterprises in the Making of Taiwan’s Economy, 1950-1985* (Cambridge, MA: Harvard University Press, 2005).

Square uprising in 1989.<sup>71</sup> Another body of work investigates the networks between top Chinese leaders and political elites or between them and local leaders, linking competition among elite groups to outcomes such as economic policy-making, political promotion, and the future composition of the Party leadership.<sup>72</sup> Others look at groups of Chinese leaders, such as the Central Committees of the CCP, and analyze changing trends in their members' demographic characteristics, such as age, ethnicity, birthplace, education, and professional and family background.<sup>73</sup> Still other analyses focus on elite contestation in particular policy areas, such as agriculture.<sup>74</sup> These studies offer important insights into the factors that affect policy-making and political mobility across levels of government in China and the processes by which both occur. However, they leave important questions unanswered, such as why predictors of

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<sup>71</sup> Frederick C. Teiwes, "The Study of Elite Political Conflict in the PRC: Politics Inside the 'Black Box'" in *Handbook of the Politics of China*, ed., David S. G. Goodman (Northampton, MA: Edward Elgar Publishing, 2015). Such works on the Great Leap Forward include: David Bachman, *Bureaucracy, Economy, and Leadership in China: The Institutional Origins of the Great Leap Forward* (New York: Cambridge University Press, 2006); Frederick C. Teiwes and Warren Sun, *China's Road to Disaster: Mao, Central Politicians, and Provincial Leaders in the Unfolding of the Great Leap Forward, 1955-1959* (Armonk, NY: M.E. Sharpe, 1999); Dali L. Yang, *Calamity and Reform in China: State, Rural Society, and Institutional Change Since the Great Leap Famine* (Palo Alto, CA: Stanford University Press, 1996). On the Cultural Revolution: Hong Yung Lee, *The Politics of the Chinese Cultural Revolution: A Case Study* (Berkeley, CA: University of California Press, 1980). On the Tiananmen Square uprising: Joseph Torigian, "Prestige, Manipulation, and Coercion: Elite Power Struggles and the Fate of Three Revolutions," (Ph.D. dissertation, Massachusetts Institute of Technology, 2016).

<sup>72</sup> Sebastian Heilmann and Lea Shih, "The Rise of Industrial Policy in China, 1978-2012" (Harvard-Yenching Institute, 2013); Jing Huang, *Factionalism in Chinese Communist Politics* (New York: Cambridge University Press, 2006); Franziska Keller, "Networks of Power: An Informal Network among Chinese Communist Elites, 1982-2007," APSA 2014 Annual Meeting Paper, accessed on August 1, 2017 at: SSRN: <https://ssrn.com/abstract=2454603>; Andrew J. Nathan, "A Factionalism Model for CCP Politics," *China Quarterly* 53 (1973): 34-66; Victor C. Shih, *Factions and Finance in China: Elite Conflict and Inflation* (New York: Cambridge: Cambridge University Press, 2008).

<sup>73</sup> Cheng Li and Lynn White, "The Thirteenth Central Committee of the Chinese Communist Party: from Mobilizers to Managers," *Asian Survey* 28 (1988): 371-399; Robert A. Scalapino, ed., *Elites in the People's Republic of China* (Seattle: University of Washington Press, 1972); Jun Zhang, Qi Zhang, and Zhikuo Liu, "The Political Logic of Partial Reform of China's State-Owned Enterprises," *Asian Survey* 57, no. 3 (2017): 395-415.

<sup>74</sup> Joseph Fewsmith, "Agricultural Crisis in China," *Problems of Communism* 38, no. 6 (1988): 78-93; Frederick C. Teiwes and Warren Sun, *Paradoxes of Post-Mao Rural Reform: Initial Steps Toward a New Chinese Countryside, 1976-1981* (New York: Routledge, 2015).

political promotion for officials in Party positions do not have the same effect for those in government positions, and vice versa.<sup>75</sup> In summary, existing research does not tell us much about how the leaders involved in political competition and elite networks actually exercise political leadership within the particular government bodies, Party organs, or state-owned enterprises that they lead on a day-to-day basis.

Nor does most research on sub-national politics in China address political leadership at the organization level, although a handful of scholars do link political leadership with policy and developmental outcomes.<sup>76</sup> Studies of local officials' career trajectories and political budget cycles reveal the powerful institutional effects of the cadre management system; however, these analyses offer a limited view of local officials' political behavior.<sup>77</sup> Other works do engage political leadership at the sub-national level but ultimately downplay it in order to reach broader generalizations

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<sup>75</sup> For example, some scholars find evidence that economic performance matters most for government rather than Party positions and at lower levels of government. Eun Kyong Choi, "Patronage and Performance: Factors in the Political Mobility of Provincial Leaders in Post-Deng China," *The China Quarterly* 212 (2012): 965-981; Pierre F. Landry, Xiaobo Lü, and Haiyan Duan, "Does Performance Matter? Evaluating Political Selection along the Chinese Administrative Ladder," APSA 2014 Annual Meeting Paper, accessed on August 1, 2017 at: <http://ssrn.com/abstract=2452482>.

<sup>76</sup> For example, Domenach 1996 analyzes the role of Wu Zhipu (吴芝圃) in the events of the Great Leap Forward in Henan province. Donaldson 2009 argues that individual provincial leaders are one factor explaining Guizhou and Yunnan provinces' adoption of disparate economic strategies. Eaton and Kostka 2014 cite examples like Geng Yanbo (耿彦波), mayor of Datong in Shanxi province, to suggest that individual leaders can diffuse ideas and information across regions through their choices and actions. Shen and Tsai 2016 contend that "agent-centric factors," including "motivated and capable local leadership" and "openness to new ideas" account for Suzhou, Wenzhou, and Dongguan cities' divergent responses to the global financial crisis. Jean-Luc Domenach, *The Origins of the Great Leap Forward: The Case of One Chinese Province* (Boulder, CO: Westview Press, 1995); John A. Donaldson, "Why Do Similar Areas Adopt Different Developmental Strategies? A Study of Two Puzzling Chinese Provinces," *Journal of Contemporary China* 60 (2009): 421-444; Sarah Eaton and Genia Kostka, "Authoritarian Environmentalism Undermined? Local Leaders' Time Horizons and Environmental Policy Implementation in China," *The China Quarterly* 218 (2014): 370-371; Xiaoxiao Shen and Kellee S. Tsai, "Institutional Adaptability in China: Local Developmental Models Under Changing Economic Conditions," *World Development* 87 (2016): 107-127.

<sup>77</sup> Gang Guo, "China's Local Political Budget Cycles," *American Journal of Political Science* 53, no. 3 (2009): 621-632; Pierre F. Landry, *Decentralized Authoritarianism in China* (New York: Cambridge University Press, 2008); Samantha A. Vorthers, "Disaggregating China's Political Budget Cycles: 'Righting' the U" (working paper, forthcoming).

about ‘local governments’ or ‘local leaders.’ Take for example the study by Marc Blecher and Vivienne Shue (2001) examining Xinji municipality’s adherence to the local developmental state model through its establishment of a fur and leather trading center. The article refers to “Xinji authorities” or “municipal officials” as the main protagonist, but it also describes how Mayor Bian Qunyou convened multiple meetings and forums to push for the trading center’s creation.<sup>78</sup> The authors write that “schemes for setting up a more ambitious centre for the fur and leather trade in Xinji began to gel.”<sup>79</sup> Yet it seems unlikely that agreement on such a bold project could have been reached spontaneously, given not only potential opposition to the proposal but also the large-scale project construction, urban land acquisition, and coordination among industry producers that it entailed. Could a fur and leather trading center have been established without Mayor Bian’s support—or if he had opposed it? Might another mayor have acted differently? Similarly, the work by Meg Rithmire (2015) on divergent local property rights arrangements in China’s northeast details the critical role of mayors—Bo Xilai in Dalian, Gong Benyan in Harbin, and Mi Fengyun in Changchun—but does not single out their influence in the processes of political bargaining and moral suasion between ‘state actors’ and ‘social actors’ that she describes.<sup>80</sup> Existing scholarship on local politics in China has yet to fully engage questions of political leadership at the organization level, yet it is precisely this leadership that is responsible for both generating action plans and carrying them out.

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<sup>78</sup> Marc Blecher and Vivienne Shue, “Into Leather: State-Led Development and the Private Sector in Xinji,” *The China Quarterly* 166 (2001): 372.

<sup>79</sup> Blecher and Shue 2001.

<sup>80</sup> Meg E. Rithmire, *Land Bargains and Chinese Capitalism: The Politics of Property Rights under Reform* (New York: Cambridge University Press, 2015).

### ***Rethinking Policy Experimentation and Implementation***

Analysis of political leadership at the organization level advances existing scholarship in two areas particularly relevant to economic reform—policy experimentation and implementation. First, it suggests that the conventional ‘point to surface’ (由点到面, *you dian dao mian*) account of policy experimentation in China falls short in several ways.<sup>81</sup> Analysis using the ‘point to surface’ framework often focuses on the politics of policy experimentation and implementation by which ‘dots’ are connected with the ‘surface,’ overlooking the organizational-level processes of trial and error that occur within each of the ‘dots’ themselves. At the organization level, heads of organizations must first formulate and select among multiple strategies, build consensus for them, and endeavor to actually carry out their chosen strategy while potentially restructuring their organizations in tandem. Variation in organizations’ policy experimentation is integral to the ‘point to surface’ approach because it allows the relative success of different approaches to be compared. This variety results in significant part from political leadership; it does not derive axiomatically from organizations’ attributes, their environmental conditions, or past approaches.

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<sup>81</sup> The point to surface approach entails a policy process in which successful individual experimental points (试点, *shidian*) are generalized as models and then implemented widely across units. It can occur in two ways: 1.) when local officials, enterprises, or even individuals initiate experimentation on the ground that administrative superiors subsequently formalize and potentially expand through pilot programs; 2.) when central or local governments first design and initiate pilot programs from the top down and select pilot participants via direct designation or selection from an applicant pool. Sebastian Heilmann, “From Local Experiments to National Policy: The Origins of China’s Distinctive Policy Process,” *The China Journal* 59 (2008): 1-30. Others posit a tripartite ‘point to line to surface’ approach. For example, Hong Hu discusses an integrated ‘point, line, surface’ (点, 线, 面, *dian, xian, mian*) approach in enterprise reform experimentation and implementation. 洪虎 [Hong Hu], 《国有经济改革与企业制度创新》 [State-owned Enterprise Reform and Institutional Innovation] (Beijing: Zhonggong zhongyang dangxiao chubanshe, 1999): 262.

Second, incorporating political leadership also provides a fuller account of how policy implementation occurs and varies at the organization level. Institutions, resource endowments, and peer behavior may all shape the range of policy implementation approaches that organization heads deem possible or desirable; however, these factors do not determine which approaches are ultimately selected and how they are carried out. As Peter Nolan (1998) concludes in his study of state-owned enterprise Capital Iron and Steel Corporation (Shougang): “The contract [responsibility system] provided the *possibility* for dynamic, growth-oriented management behavior, but it did not *ensure* that this was how the Corporation would behave.”<sup>82</sup> Instead, Nolan credits the “industrial entrepreneurship” of Shougang’s head, Zhou Guanwu (周冠五), for the company’s successful implementation of the contract responsibility system.<sup>83</sup> Specifically, Zhou exercised political leadership at Shougang by redefining its organizational strategy and structure and leading employees in successive “battles” of technological upgrading.<sup>84</sup> Political leadership at the organization level helps to account for variation in policy implementation across units and over time, as different heads of similar organizations charged with carrying out

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<sup>82</sup> Emphasis in original. The contract responsibility system required enterprises to negotiate with bureaus to formulate typically three to five year contracts on specific tax rates and profit-sharing arrangements. Peter Nolan, *Indigenous Large Firms in China’s Economic Reform: The Case of Shougang Iron and Steel Corporation* (London: Contemporary China Institute, School of Oriental and African Studies, University of London, 1998): 42.

<sup>83</sup> Seiichiro Yonekura 1986 also cites the concept of “industrial entrepreneurship” to argue that Kawasaki Steel head Nishiyama Yataro, not the Ministry of International Trade and Industry, was responsible for Japan’s post-war embrace of integrated production in the steel industry. Seiichiro Yonekura, *The Japanese Iron and Steel Industry, 1850-1990: Continuity and Discontinuity* (London: Springer, 1994).

<sup>84</sup> Mr. Zhou advanced a strategy of comprehensive contracting down to the individual level, close coordination among work units, departments, and positions, and strict assessment. He also altered the company’s organizational structure by slashing the number of top-level managers and aggressively demoting or removing managers who failed to meet performance targets. Nolan 1998; Edward S. Steinfeld, *Forging Reform in China: The Fate of State-owned Industry* (New York: Cambridge University Press, 1998).



the same policy may implement it in divergent ways, and the change of a head may cause even the same organization to significantly alter its implementation approach.

Third, a political leadership approach helps to explain why organizations ignore, delay, or even subvert policy experimentation or implementation. Some contend that the essence of CCP-led rule is “integrated fragmentation,” in which the Party uses mechanisms like the cadre management system or leading small groups to achieve central goals despite confronting segregated *xitong* (系统, which are vertically-organized administrative hierarchies focused on particular issue areas), fragmented layers of subnational government, and competing interest groups.<sup>85</sup> But these integrative mechanisms do not necessarily motivate officials to seek to realize central objectives—and studying political leadership at the organization level can help to explain why. Take for example the failure of the State Council’s 1994 national pilot scheme for developing a “modern enterprise system.”<sup>86</sup> Most of the 100 pilot enterprises retained the “factory system” (工厂制, *gongchang zhi*) instead of adopting new forms of enterprise governance.<sup>87</sup> Studying political leadership suggests that an important reason for this experiment’s failure lies at the organization level. Enterprise leaders preferred their limited gains in decision-making autonomy to proactive adoption of new governance mechanisms that would formally transfer decision-

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<sup>85</sup> Brødsgaard 2012; Li 2016.

<sup>86</sup> Jiang Zemin’s Report to the National Party Congress in October 1992 called for the establishment of a ‘modern enterprise system,’ defining its characteristics as: “clearly established property rights, well-defined power and responsibility, separation of enterprise from government, and scientific management.” Jiang Zemin, Report to the National Party Congress, October 12, 1992.

<sup>87</sup> Predominant during the planned economy period, the factory system refers to the formal arrangement of enterprise governance in which the state rather than the enterprise and its leaders directed planning, production, and sales. Enterprises were in effect the “factories” of the state. On the results of the 1994 “modern enterprise system” pilot scheme, see State Economic and Trade Commission: 《国有企业改革与建立现代企业制度》 [State-owned Enterprise Reform and Establishing a Modern Enterprise System] (Beijing: Falü chubanshe, 2001): 24.

making authority from the state to the enterprise and thereby increase their personal responsibility for losses. Since the content of the center's goal of establishing a "modern enterprise system" was still highly ambiguous and at that time had not yet been linked explicitly with corporate governance, organization heads were willing to take the risk that inaction and their companies' potential failure as enterprise pilots could adversely affect their political futures.

Fourth, analysis of political leadership at the organization level expands the standard center-local framework for studying policy experimentation and implementation in China. Within China's nested policy-making process, the center's primary function is typically understood as policy-making, not policy experimentation and implementation. Research on policy experimentation and implementation is primarily situated at the sub-national level—provinces, municipalities, counties, or townships—where much of these activities indeed take place.<sup>88</sup> However, central-level organizations and their leaders also possess bounded autonomy to engage in policy experimentation and implementation. Take for example the State Council's launch of a central-level experimental pilot during the early 1980s on the development of 'general companies' (总公司, *zonggongsi*)—large corporate entities linking multiple factories across provincial lines. It ultimately established approximately 120 'general

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<sup>88</sup> See, for example: Sarah Eaton and Genia Kostka, "Authoritarian Environmentalism Undermined? Local Leaders' Time Horizons and Environmental Policy Implementation in China," *The China Quarterly* 218 (2014): 359-380; Philip S. Hsu, "Deconstructing Decentralization in China: Fiscal Incentive Versus Local Autonomy in Policy Implementation," *Journal of Contemporary China* 13, no. 40 (2004): 567-599; Kevin J. O'Brien and Li Lianjiang, "Selective Policy Implementation in Rural China," *Comparative Politics* 31, no. 2 (1999): 167-186; Jinghan Zeng, "Did Policy Experimentation in China Always Seek Efficiency? A Case Study of Wenzhou Financial Reform in 2012," *Journal of Contemporary China* 24, no. 92 (2015): 338-356.

companies' under the authority of 38 ministerial agencies.<sup>89</sup> Such examples suggest that limited yet significant space exists for policy experimentation and implementation within the center itself.

Finally, examining political leadership at the organization level draws attention to informal everyday processes of policy experimentation and implementation. Heads of public sector organizations are constantly engaged in either maintaining or modifying existing strategies and organizational structures. While policy experimentation in China is often studied within the context of formal experimental schemes, informal everyday experimentation occurs widely outside of formal pilots. In some cases, everyday experimentation may precede formal policy pilots—an organization that achieved success through informal everyday experimentation may then be featured in a formal pilot where other organizations also participate and try out its approach. A famous example is Xiaogang village in Anhui province, where Yan Junchang (严俊昌) led a small group of peasants in clandestine experimentation with agricultural decollectivization before formal experimentation with the household responsibility system (包产到户, *baochan daohu*).<sup>90</sup> After the initiative succeeded in dramatically boosting Xiaogang's agricultural production, the village was then tapped

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<sup>89</sup> Chen Li, *China's Centralized Industrial Order: Industrial Reform and the Rise of Centrally Controlled Big Business* (New York: Routledge, 2014): 50.

<sup>90</sup> The household responsibility system in agriculture required households to meet fixed production quotas but permitted them to sell what they produced beyond the quota and retain a portion of the profits. Yan Junchang was the leader of Xiaogang's production team (生产队, *shengchan dui*). For Yan's recollections, see 《南方都市报》 [Southern Metropolis Daily], ed., 《为了不饿死，冒死“包产到户”》 [In Order Not To Starve to Death, Risking Death “Household Responsibility System”], 《中国改革开放三十年口述史》 [China's Reform and Opening Up 30 Years Oral History] (Guangzhou: Guangdong jiaoyu chubanshe, 2008). For a narrative account of Xiaogang Village's reform experience, see Chapters 1 and 2 in 陈桂棣 [Chen Guidi], 春桃 [Chun Tao] 《小岗村的故事》 [The Story of Xiaogang Village] (Beijing: Huawen chubanshe, 2009).

to participate in a formal pilot program with other localities in Anhui and Sichuan; experimentation with household responsibility reform was later gradually expanded until it was implemented nationwide.

Similarly, policy implementation efforts (or lack thereof) are an everyday process that occurs at the organization level. Yet studies of policy implementation often focus on assessing formal implementation outcomes after a given period of time. For example, a researcher might look at how many state-owned enterprises have restructured as limited liability companies or joint stock companies in the first year or five years after Jiang Zemin's Report to the 1992 National Party Congress directed state-owned enterprises to restructure and the 1993 Company Law legalized these organizational forms. Such an approach helps to index the pace and extent of policy implementation, but it offers little insight into the process by which organizations actually implement particular policies and the incentives and constraints that may shape both their ability and willingness to do so.

### ***Obstacles to Studying Political Leadership in China***

The numerous practical obstacles to studying political leadership at the organization level in China are an important reason why such research remains scarce. First, the relative availability of information about top national leaders and their predominant influence on policy-making yield disproportionate scholarly focus on these individuals. Library shelves on both sides of the Pacific brim with titles on top leaders, such as: Mao Zedong, Zhou Enlai, Chen Yun, Deng Xiaoping, Jiang Zemin, Hu Jintao, and Xi

Jinping.<sup>91</sup> In contrast, analyses of individual officials' exercise of political leadership below the top level of national leaders are rare. They appear only infrequently in internal Party cadre study materials (干部材料, *ganbu cailiao*) or occasionally in the form of memoirs or volumes of collected works.<sup>92</sup>

Another impediment to the study of political leadership at the organization level in China is the domestic intertwining of leadership studies with political ideology and its concomitant propaganda and policy functions. National leaders from Mao Zedong to Xi Jinping have themselves published volumes of writing on their thinking about China's politics, economics and society. These works are obligatory reading for officials, to whom they are disseminated together with "important speeches" by top Chinese leaders for formal and informal study. Works of leadership thinking are sometimes even required reading for the general public, as was famously the case with Mao's "Little Red Book." The distinct leadership thought of every top leader since Mao is often referenced and in some cases even explicitly guides academic analysis of politics and the economy in China, beginning from Mao Zedong thought to Deng Xiaoping theory to Jiang Zemin's 'Three Represents' to Hu Jintao's 'Scientific

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<sup>91</sup> On Mao Zedong: Ross Terrill, *Mao: A Biography* (Palo Alto, CA: Stanford University Press, 1999); 逢先知 [Feng Xianzhi], 金冲及 [Jin Chongji], 《毛泽东传》 [Biography of Mao Zedong] (Beijing: Zhongyang wenxian chubanshe, 2003). On Zhou Enlai: Chae-jin Lee, *Zhou Enlai: The Early Years* (Palo Alto, CA: Stanford University Press, 1994). On Chen Yun: David M. Bachman, *Chen Yun and the Chinese Political System* (Berkeley, CA: University of California Berkeley, Center for Chinese Studies, 1985); 杨明伟 [Yang Mingwei], 《晚年陈云》 [Chen Yun in His Later Years] (Beijing: Xiandai chubanshe, 2015). On Deng Xiaoping: Ezra Vogel, *Deng Xiaoping and the Transformation of China* (Cambridge, MA: Belknap Press of Harvard University Press, 2011). On Jiang Zemin: Bruce Gilley, *Tiger on the Brink: Jiang Zemin and China's New Elite* (Berkeley, CA: University of California Press, 1998). On Hu Jintao: Kerry Brown, *Hu Jintao: China's Silent Ruler* (Singapore: World Scientific, 2012).

<sup>92</sup> See for example the journal 《党建研究纵横谈》 [Party-Building Research Discussion] formerly published by the Central Organization Department's Party-Building Research Institute.

Development and Harmonious Society’ and finally to Xi Jinping’s ‘Four Comprehensives.’

The CCP’s strong emphasis on collective leadership (集体领导, *jiti lingdao*) and collective decision-making (集体决策, *jiti juece*) also complicates research into organization-level political leadership in China.<sup>93</sup> Each government or Party organization in China also has a leadership group (领导班子, *lingdao banzi*) comprising the top leader and a small number of leading officials. But in practice, while heads of public sector organizations work in concert with their leadership group, they exert predominant influence on decision-making, especially major decisions like those involving organizational strategy and structure. However, enduring emphasis on collective leadership and collective decision-making may limit researchers’ ability to identify how a single individual can disproportionately influence decision-making. Organization heads may be reluctant to discuss their own political leadership in such terms, while conversely subordinates may be overly eager to give them credit.<sup>94</sup>

Finally, lack of available sources, as well as the politicized nature of some of the materials that are available, makes it difficult to study political leadership at the organization level in China. It is very hard for researchers to gain direct, repeated access to Party or government organizations—such as central ministries, local government organs, or state-owned enterprises—or to gather comprehensive quantitative or qualitative data about their internal operations, because these are

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<sup>93</sup> Collective leadership involves the distribution of authority and functions among government and Party organs and their leaders. Collective decision-making refers to a decision-making process that stresses discussion and the reaching of consensus among all participants.

<sup>94</sup> This may especially be the case for interviews conducted by researchers from outside the organization or by non-Chinese researchers.

official bodies with closed operations that involve restricted if not classified information.<sup>95</sup> Scholars have therefore relied heavily on analysis of decisions or policies enacted (or not enacted) by particular organizations and their leaders. Some insight into organizational leaders' thinking or the politicking surrounding particular decisions and policies can be gained through official compendiums of their speeches and/or selected writings (选集, *xuanji*), records of interviews (访谈录, *fangtan lu*), or memoirs (回忆, *huiyi*) by them or by their close aides, all of which are typically published late in life. However, these materials are limited in scope, rarely engage in direct criticism or recount instances of conflict, and are often either compiled directly by official organs or subject to censors' review, thereby further increasing the risk of potential bias.

### ***Conclusion***

This chapter has proposed a political leadership approach to studying economic reform in China. It argues that heads of public sector organizations—government bodies, Party organs, and state-owned enterprises—possess bounded autonomy to influence reform policy experimentation and implementation. These individuals exercise political leadership in two main ways: by determining the specific strategies of the organizations that they lead, and by altering their structures. A political leadership

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<sup>95</sup> A small number of scholars have been able to gain in-depth access to Chinese organizations; however, most have been market rather than government or Party organizations. They include: Amy Hanser, *Service Encounters: Class, Gender, and the Market for Social Distinction in Urban China* (Palo Alto, CA: Stanford University Press, 2008); Ellen Hertz, *The Trading Crowd: An Ethnography of the Shanghai Stock Market* (Cambridge: Cambridge University Press, 1998); Ching Kwan Lee, *Gender and the South China Miracle: Two Worlds of Factory Women* (Berkeley, CA: University of California Press, 1998); Lu Zhang, *Inside China's Automobile Factories* (New York: Cambridge University Press, 2014).

approach emphasizes choice within organizational and institutional constraints, instead of assuming that organizational and institutional constraints largely determine behavioral and policy outcomes. By focusing on the heads of organizations, a political leadership approach also highlights the hierarchies of influence that operate within and among organizations. Organizational and institutional constraints do not restrict all actors equally, and actors have varying abilities to maintain or to modify them.

Research on China's politics and economy needs to take heads of public sector organizations seriously as political leaders. "Political leadership" describes the functions that many of these individuals perform: engaging in experimentation, formulating strategies, restructuring their organizations, and influencing others to follow the directions that they set. However, scholars typically reserve this term for analysis of national leaders; it is rarely applied to officials below or even at the ministerial level. Yet even studies that address top officials typically focus on leaders as individuals (the biographical approach) or groups of political elites (the elite politics approach), rather than examining their actual exercise of leadership within the particular organizations they lead and its policy impact. Research on sub-national politics tends to either view organizational leaders as managers subordinate to administrative authorities or to de-emphasize their influence in order to reach broader conclusions about 'local governments.'

Studying political leadership at the organization level advances extant research on reform policy experimentation and implementation in China in multiple ways. It suggests that political leadership is an important driver of variation in both policy experimentation and implementation. A political leadership approach can also help to



explain why some organizations ignore, delay, or subvert policy experimentation or implementation, even within the same institutional context. It expands the standard center-local framework for studying policy experimentation and implementation in China, by showing that central-level organizations and their leaders too possess limited yet significant space to engage in policy experimentation and implementation. Finally, it calls attention to organizational leaders' role in catalyzing and guiding the informal everyday processes of policy experimentation and implementation that occur widely outside of formal pilots, and that in some cases even precede them.

## Chapter 2

### **Creating and Expanding Space for Political Leadership:**

#### **Enterprise Reform Policies Since 1978**

This chapter describes how enterprise reform policies in China's state-owned economy since 1978 first created and then expanded space for political leadership at the organization level. Over the past four decades, heads of state-owned enterprises have gone from managing production to determining how to restructure their organizations and promote their development in both domestic and international markets. After the establishment of the State-owned Assets Supervision and Administration Commission (SASAC) in 2003, its heads too exercised political leadership by setting specific strategies to achieve the center's goals for the state-owned economy and by altering the organizational structure of the state-owned enterprises under its administration. Close analysis of enterprise reform policies illuminates the origins and changing contours of these officials' bounded autonomy to exercise political leadership at the organization level.

Focus here on central-level enterprise reform policies should not be read as corroboration of a strategic design perspective's claim that economic reform is a top-down process. Top national leaders and political elites' choices about enterprise reform policies and experimentation did significantly shape both organizational change and the institutional evolution of state ownership. But the dynamics of organizational and institutional change extended much further than this. Enterprise reform policies initiated by top national leaders and the State Council also created and

expanded space for organization heads to influence policy experimentation and implementation. Organizational change wrought by these individuals' political leadership also fed back into enterprise reform policies and influenced the institutional evolution of state ownership. The center provides the "initial trigger for the co-evolution" between the micro and macro levels, but subsequent policy and institutional change then become an interactive process in which the heads of public sector organizations also play a significant role.<sup>96</sup>

In particular, this chapter highlights the series of enterprise reform policies behind the emergence of China's "national champions"—the central state-owned enterprises that are the focus of this dissertation. Initial attempts to build large centrally-owned, multi-region and multi-production unit corporations began as early as 1981 with the State Council's establishment of 'general companies' under central ministries. These efforts gained momentum with the launch of national-level pilots to develop large state-owned enterprise groups in 1991 and Jiang Zemin's endorsement of a reform strategy of "grasping the large and releasing the small" in 1995. During the second half of the 1990s, the center sought to forge internationally competitive national firms through enterprise policies supporting their "going out" and partial public listing of assets on domestic and overseas stock exchanges. These efforts culminated with the creation of SASAC in 2003 as a government ownership agency responsible for administering a portfolio of central state-owned enterprises.

In the following discussion, I divide enterprise reforms since 1978 into four periods: the emergence and decline of 'dual track' economic reform (1978-1991),

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<sup>96</sup> Barbara Krug and Hans Hendrichske, "Framing China: Transformation and Institutional Change through Co-evolution," *Management and Organization Review* 4, no. 1 (2008): 84.

establishment of a socialist market economy (1992-1994), retrenchment of state ownership in the “commanding heights” (1995-2001), and internationalization and consolidation of the state sector (2002-present). For each period, I first summarize key enterprise reform policies—their content, implementation, and results (Table 2.1). I then discuss how these enterprise reform policies affected space for organizational leaders in the state-owned economy to exercise political leadership. While this chapter is not the first to provide an overview of post-1978 enterprise reforms in China, it extends existing accounts by examining reform policies in the state-owned economy during the past decade and examining previously untapped source materials.<sup>97</sup> The analysis uses qualitative data from elite interviews conducted in Beijing in 2016 and an extensive body of Chinese language sources, some of which have never been used before, including: official policy documents, government statistics, internal government journals, writings and memoirs of Chinese officials and economists, economic reform yearbooks, newly declassified U.S. State Department cables, and secondary sources.<sup>98</sup>

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<sup>97</sup> Seminal works on economic reform in China’s state-owned economy give a comprehensive account of enterprise reform policies but end their analysis in 1993. Barry Naughton, *Growing Out of the Plan: Chinese Economic Reform, 1978-1993* (Cambridge: Cambridge University Press, 1996); Susan L. Shirk, *The Political Logic of Economic Reform in China* (Berkeley, CA: University of California Press, 1993). Two recent works that do examine state-owned enterprise reforms during the past decade do so from the perspectives of ideational and bureaucratic contestation, respectively. Sarah Eaton, *The Advance of the State in Contemporary China: State-Market Relations in the Reform Era* (Cambridge: Cambridge University Press, 2015); Chen Li, *China’s Centralized Industrial Order: Industrial Reform and the Rise of Centrally Controlled Big Business* (New York: Routledge, 2014).

<sup>98</sup> I gathered these sources in Beijing and Hong Kong during 24 months of dissertation fieldwork between 2013 and 2016 and supplemented them with additional materials from the Fairbank Center Collection of the Fung Library and the Harvard-Yenching Library in 2017.

Table 2.1: Key Enterprise Reforms in China Since 1978

| Period   | Enterprise reforms (start dates)  |
|--|---|
| <b>Emergence and decline of ‘dual track’ economic reform (1978-1991)</b>       | Expanding enterprise autonomy (1978)<br>Economic responsibility system (1981)<br>‘General companies’ (1981)<br>Tax-for-profit (1983)<br>Contract responsibility system (1987)<br>Enterprise groups (1991) |
| <b>Establishment of a socialist market economy (1992-1994)</b>                 | Shareholding system restructuring (1992)<br>Separating government from enterprises (1992)   |
| <b>Retrenchment of state ownership in the “commanding heights” (1995-2001)</b> | Grasping the large and releasing the small (1995)<br>Partial public listing of large industrial state-owned enterprise assets (1997)  |
| <b>Internationalization and consolidation of the state sector (2002 on)</b>    | Corporate governance (1999)<br>“Going out” (2002)<br>Creation of SASAC and central state-owned enterprises (2003)   |

### ***Emergence and Decline of ‘Dual Track’ Reform (1978-1991)***

Companies (公司, *gongsi*) did not exist in China at the start of the reform period. The state-owned economy consisted of groups of wholly state-owned and state-run factories (工厂, *gongchang*) embedded in the multi-level administrative hierarchies of particular industrial bureaus. These factories were not companies but rather production units: they had little decision-making authority for operations or responsibility for performance. Bureaus determined factories’ production methods, inventory levels, and product distribution; oversaw their daily operations; and participated in recruiting

managers and employees as well as their training, discipline, and housing allocation.<sup>99</sup>

If a factory did not meet its production quota, the bureau would make up for it by drawing from other production units under its supervision. Only with the advent of market-oriented reforms in 1978 would state-owned factories begin their long journey toward becoming first “state-run enterprises” (国营企业, *guoying qiye*) and then “state-owned enterprises” (国有企业, *guoyou qiye*).

Early enterprise reform upheld the dominance of state ownership and the economic planning system, while simultaneously introducing market mechanisms into enterprises and granting them limited operational autonomy. This combination of plan and market is popularly known as China’s ‘dual track’ (双轨制, *shuang gui zhi*) approach to economic reform. However, the plan itself changed too in the ‘dual track’ approach. Central planning evolved from top-down mandates and administrative compulsion to bargaining between planning authorities and enterprises to determine contractual assignment of enterprise responsibility for production targets, and finally the replacement of administrative methods with indirect guidance using economic instruments such as taxes, interest rates, and credit allocation.<sup>100</sup> The following sections summarize key early enterprise reforms: expansion of enterprise autonomy (1978), the economic responsibility system (1981), ‘general companies’ (1981), tax-for-profit reforms (1983), the contract responsibility system (1987), and enterprise groups (1991).

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<sup>99</sup> Lisa A. Keister, *Chinese Business Groups: The Structure and Impact of Interfirm Relations during Economic Development* (Oxford: Oxford University Press, 2000): 54.

<sup>100</sup> Donald Hay, Derek Morris, Guy Liu, and Shujie Yao, *Economic Reform and State-Owned Enterprises in China: 1979-87* (Oxford: Oxford University Press, 1994): 19.

### *Expanding Enterprise Autonomy (1978)*

Initial enterprise reforms sought to expand enterprise autonomy (*kuoda qiye zizhu quan*) by power-delegation and profit sharing (放权让利, *fangquan rangli*): granting state firms greater decision-making authority over their operations and permitting them to retain a percentage of their profits. Enterprises were granted limited autonomy over input sourcing, production, sales, investment, and compensation.<sup>101</sup> Goods produced in excess of the central plan could be sold on the market and enterprises permitted to retain a fixed percentage of additional profits earned. Enterprises could then reinvest retained profits into infrastructure or equipment, or use them to incentivize employees through bonuses or service provision. In theory, granting enterprises more autonomy over operations and earnings would prompt them to become more responsive to market competition and to develop independent economic interests.

In October 1978, Zhao Ziyang launched a pioneering pilot program to expand the operational autonomy of six state-owned factories in Sichuan province. Following its success, the Sichuan government expanded the program to 100 industrial enterprises and 40 commercial enterprises in January 1979, and then again to 417 industrial enterprises and 250 commercial enterprises in 1980.<sup>102</sup> In addition, six central ministries and commissions—including the State Economic Commission and

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<sup>101</sup> For example, the state authorized enterprises to modify central plans regarding product types and variety if they did not meet market needs. 邵宁 [Shao Ning]: 《国有企业改革实录》 [The Reform of State-owned Enterprises in Memoir] (Beijing: Jingji kexue chubanshe, 2014): 10-11.

<sup>102</sup> 王海波 [Wang Haibo], ed., 《工业经济史》 [Industrial Economics History] (Beijing: Jingji guanli chubanshe, 1986): 436.

the Ministry of Finance—chose eight enterprises in Beijing, Tianjin, and Shanghai to pilot enterprise autonomy reforms starting in May 1979.<sup>103</sup>

The State Council quickly expanded enterprise autonomy pilots nationwide. On July 13, 1979, the State Council released “Several Provisions on Expanding the Autonomy of State-owned Industrial Enterprises” together with four other policy documents—its first set of policy directives on state-owned enterprise reform.<sup>104</sup> With these policy directives, the State Council expanded enterprise autonomy reforms to 1,590 industrial enterprises in 26 provinces, municipalities, and autonomous regions.<sup>105</sup> As the reform achieved initial success, the State Council further expanded enterprise autonomy reforms in June 1980 to more than 6,600 state-owned enterprises nationwide (constituting approximately 16% of all state-owned industrial enterprises). With 5,777 pilot enterprises reporting from 28 provinces, municipalities, and autonomous regions, in 1980 these enterprises achieved increases of 6.9% in the value of state-owned assets, 11.8% in profits, and 7.4% in remitted profits compared to the previous year.<sup>106</sup>

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<sup>103</sup> These pilot enterprises included Shougang Iron and Steel [首都钢铁], Shanghai Diesel Engine Factory [上海柴油机厂], Tianjin Bicycle Factory [天津自行车厂], and Sichuan Ningjiang Machine Tool Plant [四川宁江机床厂]. See also Justin Yifu Lin, Fang Cai, and Zhou Li, *State-owned Enterprise Reform in China* (Hong Kong: Chinese University Press, 2001): 53.

<sup>104</sup> State Council: 《关于扩大国营工业企业经营管理自主权的若干规定》 [Several Provisions on Enlarging the Autonomy of State-owned Industrial Enterprises], July 13, 1979; State Council: 《关于国营企业实行利润留成的规定》 [Provisions on Implementing the Retention of Profits of State-owned Enterprises], July 13, 1979; State Council: 《关于开征国营企业固定资产税的暂行规定》 [Interim Provisions on Administering Fixed Assets Tax on State-owned Enterprises], July 13, 1979; State Council: 《关于提高国营工业企业固定资产折旧率和改进折旧费使用办法的暂行规定》 [Interim Provisions on Measures to Improve the Depreciation Rate of Fixed Assets of State-owned Industrial Enterprises and the Use of Depreciation Fees], July 13, 1979; State Council: 《关于国营工业企业实行流动资产全额信贷的暂行规定》 [Interim Provisions on State-owned Industrial Enterprises' Implementation of Full Credit of Current Assets], July 13, 1979.

<sup>105</sup> Wang 1986: 437.

<sup>106</sup> Wang 1986: 438.



However, mounting fiscal deficits and inflation throughout 1980 raised fears among conservatives in the top leadership and dampened enthusiasm for enterprise autonomy reforms.<sup>107</sup> China experienced historically unprecedented fiscal deficits of 17 billion RMB in 1979 and 12.1 billion RMB in 1980, while the consumer price index rose 1.9% in 1979 and then soared 6% in 1980.<sup>108</sup> As fears rose among some in China's top leadership that the economy was out of control, Chen Yun led calls to readjust the national economy (调整国民经济, *tiaozheng guomin jingji*) by reviving centralized economic planning. In December 1980, the Central Work Conference—led by Chen Yun—announced plans for a “clearheaded” and “healthy” adjustment of the national economy” beginning in 1981.<sup>109</sup> However, enterprise autonomy reforms would soon reemerge in a different form.

#### *Economic Responsibility System (1981)*

Economic responsibility system (经济责任制, *jingji zeren zhi*) reforms sought to further clarify the rights, interests, and responsibilities of state-owned enterprises vis-à-vis the state. They required enterprises to negotiate individually with government bureaus on an annual basis to establish specific targets, profit retention rates, and responsibility for shortfalls or losses.<sup>110</sup> Economic responsibility reforms also aimed to

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<sup>107</sup> For discussion of problems specific to the reforms, see Naughton 1995: 103-105.

<sup>108</sup> 章迪诚 [Zhang Dicheng], ed., 《中国国有企业改革编年史, 1978-2005》 [Chronicle of China's State-owned Enterprise Reform] (Beijing: Zhongguo gongren chubanshe, 2006): 61.

<sup>109</sup> 陈云 [Chen Yun]: 《经济形势与经验教训》 [Economic Situation and Lessons Learned], speech at the Central Work Conference, December 16, 1980.

<sup>110</sup> The state implemented three main types of power-delegation and profit-sharing arrangements: 1.) ‘profit retention’ (利润留成, *lirun liucheng*) arrangements, which permitted enterprises to retain a significant percentage of profits (typically not more than 40%) for goods produced and sold above planned targets; 2.) ‘profit and loss’ (盈亏包干, *yingkui baogan*) arrangements, which allowed

specify the rights, interests, and responsibilities of state-owned enterprises vis-à-vis their employees. Enterprises now needed to make comprehensive budgets taking into account factors like input and equipment costs, planned sales volumes and revenues, liabilities, and employee compensation and benefits. They also had to clarify position responsibilities and performance assessment standards and to devise remuneration systems linking employee compensation with individual and enterprise performance.<sup>111</sup> These changes strengthened incentives for enterprise heads to make profit-oriented investment decisions and boosted employee productivity and efficiency. However, enterprises at the same time pressed vigorously for reductions in their output plan targets and/or price increases for their outputs.<sup>112</sup>

Changes in China's top economic leadership at the beginning of the 1980s enabled widespread implementation of economic responsibility system reforms. In 1980, Zhao Ziyang took over leadership of the Economic Leading Group from Chen Yun, who formally retired. In April 1981, the State Council-organized "National Industry and Transportation Work Conference" in Shanghai proposed implementing the economic responsibility system in industrial enterprises. Subsequent policy documents released in October and November 1981 clarified the content and

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enterprises to retain profits above a certain amount but also mandated they take responsibility for shortfalls or losses above a fixed amount; 3.) 'tax-for-profit, self-responsibility for profit and loss' (以税代利、自负盈亏, *yi shui dai li, zifu yingkuai*) arrangements, which substituted taxes for profit remittance, allowed partial profit retention, and required enterprises assume full responsibility for losses. The majority of enterprises adopted 'profit and loss' arrangements. Shao 2014: 14-15.

<sup>111</sup> For discussion of the different types of remuneration systems developed, see Shao 2014: 15.

<sup>112</sup> The two-tiered system of market and plan also incentivized agents to divert goods from plan to market to obtain the 'rents' embodied in the goods due to administrative controls. William Byrd, "The Market Mechanism and Economic Reforms in Chinese Industry" (Ph.D. dissertation, Harvard University, 1987): 432.

principles of the reforms.<sup>113</sup> Between 1981 and 1982, more than 30,000 state-owned industrial enterprises nationwide (constituting approximately 80% of all state-owned industrial enterprises) implemented enterprise responsibility reforms.<sup>114</sup>

Economic responsibility reforms initially succeeded in reducing debt and increasing productivity, but their shortcomings soon became apparent. After the first year of nationwide implementation, the national fiscal deficit decreased from 12.7 billion RMB in 1980 to 2.5 billion RMB in 1981.<sup>115</sup> But the state's fiscal revenues (enterprise revenues plus tax revenues) increased only gradually—from 1.16 billion RMB in 1980 to 1.18 billion RMB in 1981 and finally to 1.21 billion RMB in 1982—while enterprise profit retention rates rose steadily during this period.<sup>116</sup> This was primarily because enterprise heads exploited the information asymmetries inherent in their one-on-one bargaining with the state, while significant latitude for adjustment weakened the reform's intended incentive effects.<sup>117</sup>

#### *'General Companies' (1981)*

Experimentation with the establishment of 'general companies' (总公司, *zonggongsi*) marked the Chinese leadership's first effort to develop large industrial conglomerates

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<sup>113</sup> State Council: 《关于实行工业生产经济责任制若干问题的意见》 [Opinions on Several Issues Concerning Implementation of the Economic Responsibility System for Industrial Production], October 29, 1981; State Council: 《关于实行工业生产经济责任制若干问题的暂行规定》 [Interim Provisions on Several Issues Concerning Implementation of the Economic Responsibility System for Industrial Production], November 11, 1981.

<sup>114</sup> Wang 1986: 442.

<sup>115</sup> Zhang 2006: 63.

<sup>116</sup> Multiple years of China Statistical Yearbook, as cited in Yijia Jing, "Creative Incrementalism: Governance Reforms in China Since 1978," *Chinese Political Science Review* 2, no. 1 (2017): 56-68.

<sup>117</sup> For example, enterprise heads strategically exploited this information asymmetry by underreporting profits or concealing enterprise capabilities in order to negotiate for lower production targets.

during the reform era.<sup>118</sup> The center envisioned that ‘general companies’—large corporate entities linking multiple factories across provincial lines—would not only amalgamate the assets and employees of separate production units, but also their supply networks, affiliated training facilities, and relevant industry research and design institutes. Beginning in 1978, Chinese policymakers advocated importing advanced technology from abroad and closely studied the examples of foreign multinationals from the United States, Japan, and Western Europe. However, the primary aim of ‘general company’ development, like that of state ownership, remained domestic development after the lost decade of the Cultural Revolution.

‘General companies’ achieved initial success before foundering on resistance from multiple fronts. By the end of 1982, the State Council had established approximately 120 nationwide industrial ‘general companies’ under the authority of 38 ministerial agencies.<sup>119</sup> However, local governments were reluctant to give up the control and revenues from local production units that were to be combined into the new ‘general companies.’ And local production units themselves, many of which had distinct interests and region-based identities, were unenthusiastic about being integrated into a unitary general company, subject to the authority of a distant company headquarters. Moreover, as the decade went on, the structure and operation of ‘general companies’ appeared increasingly incongruent with Premier Zhao Ziyang’s

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<sup>118</sup> It revived the aim of the short-lived ‘corporate trust’ (托拉斯, *tuolasì*) experiments that Liu Shaoqi, Bo Yibo, and Deng Xiaoping pioneered in the early 1960s. In this earlier pilot, 12 centrally controlled corporate trusts were established in 1964, including 12 nationwide pilot enterprises and 3 regional pilot enterprises. After foundering on opposition from local governments and local enterprises, the outbreak of the Cultural Revolution abruptly ended experimentation. Li 2014: 47.

<sup>119</sup> Two of them—China Petrochemical Corporation (Sinopec) and China Shipbuilding Industrial Corporation—held full ministerial rank. Li 2014: 50.

policy emphasis on decentralizing authority to local governments and individual production units.<sup>120</sup>

### *Tax-for-profit (1983)*

Tax-for-profit (利改税, *li gai shui*) reform substituted an income tax for state-owned enterprises' profit remittance in an effort to legalize enterprises' economic responsibility to the state while making them more accountable for both profits and losses.<sup>121</sup> The State Council carried out the reform in two main stages.<sup>122</sup> The first stage in April 1983 mandated that state-owned enterprises pay a flat income tax of approximately 55% of their profit target.<sup>123</sup> The second stage of the reform began in September 1984 when the State Council released a policy document calling for nationwide implementation of tax-for-profit reforms; the Decisions of the Third Plenum the following month affirmed the reform's widespread implementation.<sup>124</sup>

However, the hasty implementation of tax-for-profit reform ended in failure—after its initiation, state-owned enterprise profits declined for 22 consecutive

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<sup>120</sup> Li 2014: 51-52.

<sup>121</sup> The State Council also had two broader aspirations for tax-for-profit reform. First, tax-for-profit reform was to be enacted together with producer goods price adjustments, so that uniform tax rates could be imposed across industries and a standardized, impartial tax system could begin to develop. It also envisioned that the tax-for-profit reform would serve as the foundation for a new system of dividing central-local revenues, in which some taxes would be designated as 'central revenues' and some as 'local revenues.' Naughton 1995: 183.

<sup>122</sup> The earliest efforts began in 1980 with a trial group of 10 state-owned enterprises (later expanded to 400) in three provinces—Shanghai, Sichuan and Guangxi. Hays et al 1994: 23.

<sup>123</sup> In addition, a small number of more profitable state firms were also required to pay an additional "adjustment tax" (调节税, *tiaojie shui*): an additional variable percentage of their after-tax profits. State Council: 《关于国营企业利改税试行办法》 [On Trial Measures for Tax Reform of State-owned Enterprises], April 24, 1983.

<sup>124</sup> See State Council: 《关于在国营企业推行'利改税'第二步改革的报告》 [Report on Carrying Out Tax-for-Profit Reform in State-owned Enterprises Reform Phase Two], September 18, 1984. Central Committee of the Communist Party of China: 《中共中央关于经济体制改革的决定》 [Decision of the Central Committee of the Communist Party of China on Economic Reform], October 21, 1984.

months.<sup>125</sup> Substituting taxes for profit could not replace the need for price reform: enterprises' profitability derived from pricing, not just from efficiency. Moreover, profitability was an inappropriate yardstick to measure the performance of state-owned enterprises that were public utilities or education, health, or transportation providers. Enterprise implementation was slow and often superficial, as enterprise heads altered previous economic responsibility systems to make them look like tax-for-profit reforms or underreported profits in order to protect retained earnings. Clashes among divergent interests also weakened the tax-for-profit reforms ultimately implemented. Some opposed increasing enterprises' economic burdens (the State Economic Commission and local officials), while others wanted to ensure central government revenues (the Ministry of Finance).<sup>126</sup> Struggle to formulate tax-for-profit reforms also reflected the top-level split between Premier Zhao Ziyang (who advocated tax-for-profit reform) and Communist Party of China General Secretary Hu Yaobang (who favored a contracting approach).<sup>127</sup> When tax-for-profit reform ended in failure, enthusiasm began to stir again for a profit contracting approach to enterprise reform.

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<sup>125</sup> Zhang 2006: 110.

<sup>126</sup> More than 20 drafts of plans for the second stage of tax-for-profit reforms were prepared during 1984, reflecting the intense bargaining during its formulation. Naughton 1995: 184.

<sup>127</sup> Shirk 1993: 246. For a summary of the politics behind the formulation of the tax-for-profit reform, see Chapter 12, "Building Bureaucratic Consensus: Formulating the Tax-for-Profit Policy, 1983-1984," Shirk 1993.

### *Contract Responsibility System (1987)*

Contract responsibility system (承包责任制, *chengbao zeren zhi*) reform was the final major enterprise reform effort before the political and economic turmoil of 1989.<sup>128</sup> It differed from the previous economic responsibility system reform because bureaus negotiated contracts with specific tax rates and profit-sharing arrangements with individual enterprises on a longer-term basis (typically three to five years) instead of every year. Enterprise heads had more risk because they had to formulate longer-term strategic plans and confront market changes, like increased input costs, without the possibility of bargaining every year to modify contract targets. If an enterprise failed to meet its targets, its managers would now literally pay the price by losing their jobs and even security deposits of their own money.<sup>129</sup> However, enterprise heads also enjoyed more potential reward, because they gained autonomy over medium-term enterprise operations and allocation of profits generated ‘above the plan.’

The Chinese leadership identified widespread implementation of the contract responsibility system as the top reform priority for 1987.<sup>130</sup> By the end of that year, more than 78% of all industrial enterprises in the central plan had implemented the

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<sup>128</sup> The contract responsibility system had varied forms united by a shared set of principles: contracting for a fixed base amount, ensuring the turning over of profits, permitting enterprises to retain excess profit, and requiring them to cover any shortages themselves (包死基数, 确保上交, 超收多留, 欠收自补, *baosi jishu, quebao shangjiao, chaoshou duoliu, qianshou zibu*). State Economic Commission, State Economic Restructuring Commission: 《关于深化企业改革, 完善承包经营责任制的意见》 [Opinions on Deepening Enterprise Reform and Refining the Contract Responsibility System], August 28, 1987.

<sup>129</sup> According to the World Bank Enterprise Survey conducted between 1991 and 1992, approximately 20% of contract signatories in state-owned enterprises reported committing collateral, with an average payment of 14,258 RMB. Gary H. Jefferson and Inderjit Singh, *Enterprise Reform in China: Ownership, Transition, and Performance* (New York: Oxford University Press, 1998): 54. See also Theodore Groves, Yongmiao Hong, John McMillan, and Barry Naughton, “China’s Evolving Managerial Labor Market,” *Journal of Political Economy* 103, no. 4 (1995): 879.

<sup>130</sup> 《政府工作报告(1987年)》 [Government Work Report (1987)], March 25, 1987.

contract responsibility system, including 82% of all medium and large state-owned enterprises.<sup>131</sup> Combined profits and taxes for industrial enterprises in the national budget reached 36.9 billion RMB by the end of 1988, equivalent to the total amount of industrial enterprises' profits and taxes for the entire six years between 1981 and 1986.<sup>132</sup> However, the problems of moral hazard and soft budget constraint persisted, because managers in the state-owned economy assumed responsibility for gains but not for losses. At the same time, government agencies grew frustrated as state-owned enterprise leaders' information asymmetry and low baselines locked in at contract signing meant that many contracts ended up being highly favorable to enterprises.

### *Enterprise Groups (1991)*

Following the economic and political turmoil of 1989, China sought to revive the state-owned economy by promoting the development of state-owned enterprise groups (企业集团, *qiye jituan*). Like 'general companies,' enterprise groups were also large multi-region, multi-production unit corporate entities.<sup>133</sup> But enterprise groups started from large production units (which constituted the 'core enterprises' of a given enterprise group) at a lower level of the production system under central ministries, rather than originating from central ministry headquarters or even directly from the State Council itself.<sup>134</sup> Beyond the reform's myriad economic objectives, Chinese leaders embraced enterprise groups as a strategic solution to the political dilemma of

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<sup>131</sup> Zhang 2006: 177.

<sup>132</sup> Ibid.

<sup>133</sup> A business group comprises a coalition of separate enterprise units, each an independent legal entity, connected through varying legal, economic, and social ties, and typically spanning multiple industries. See Keister 2000: 26-29.

<sup>134</sup> Li 2014: 64.



economic reform: how to maintain social stability and state control over the economy while advancing economic development.<sup>135</sup>

Enterprise group reform began in earnest with a national-level pilot in December 1991 but was not expanded more widely until later in the decade.<sup>136</sup> That month, “Announcement of Guidance on the Selection of a Batch of Large Enterprise Groups for Experimental Pilots” named 55 pilot enterprises under 12 different central industrial ministries.<sup>137</sup> The State Council oversaw enterprise group reforms while the Chinese Communist Party’s Central Organization Department appointed their top leaders.<sup>138</sup> However, multiple problems beset pilot enterprise groups: weak economic performance and even losses, lack of cohesion between the holding company and

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<sup>135</sup> See Chapter 2, “The Ideas Behind the Advance of the State,” Eaton 2015. These economic objectives included: improving the performance of the state-owned economy and enterprises alike by creating economies of scale and specialization to cut costs and boost competitiveness; pooling scarce labor and capital resources among member enterprises to develop new technology and products; protecting member enterprises from competition by creating larger industry players; reducing pressure on state banks and potential employee layoffs by merging struggling state-owned enterprises with stronger performers; and making government macro-economic adjustment more effective. 洪虎 [Hong Hu], 《国有经济改革与企业制度创新》 [State-owned Enterprise Reform and Institutional Innovation] (Beijing: Zhonggong zhongyang dangxiao chubanshe, 1999); Keister 2000.

<sup>136</sup> These efforts followed a decade of informal experimentation and discussion about enterprise groups. See State Council: 《关于推动经济联合的暂行规定》 [Provisional Regulations Regarding the Promotion of Economic Alliances], July 1, 1980; State Council: 《关于进一步推动横向经济联合若干问题的规定》 [Regulations Regarding a Few Issues Related to the Further Promotion of Lateral Economic Alliances], March 23, 1986; State Council: 《关于深化企业改革增强企业活力的若干规定》 [Several Provisions on Deepening Enterprise Reform and Strengthening Enterprise Vitality], December 5, 1986; State Economic Restructuring Commission and the National Committee on Economic Alliances: 《关于组建和发展企业集团的几点意见》 [A Few Ideas Regarding the Establishment and Development of Business Groups], December 16, 1987.

<sup>137</sup> The State Council later expanded the number of pilot enterprises to 56 with the removal of East Coal Group [东煤集团] and the addition of China Guangdong Nuclear Power Group [中国广东核电集团] and China Gezhouba Water Conservancy and Hydropower Engineering Group [中国葛洲坝水利水电工程集团].

<sup>138</sup> In 1994, the Central Organization Department accorded top leaders in 31 of the pilot enterprises the equivalent of vice-ministerial rank, reflecting these firms’ growing political as well as economic importance. For a list of these firms, see Central Organization Department, Ministry of Personnel: 《关于部分国家试点企业集团主要领导成员享有副部级政治待遇问题的通知》, [Notice on the Vice-Ministerial Political Treatment of the Top Leaders of Some National Pilot Enterprise Groups], November 30, 1994.

member companies, and continued government interference in enterprise groups' investment and capital raising activities.<sup>139</sup> Enterprise group reform would not achieve a major breakthrough until it became intertwined with and ultimately subsumed in the strategy of “grasping the large and letting go of the small,” discussed later in this chapter.

### *Creating Space for Political Leadership at the Organization Level*

These early enterprise reforms created new—but still very limited—space for state-owned enterprise heads to exercise political leadership at the organization level. For the first time, state-owned enterprise heads could influence reform experimentation and implementation. They did this by bargaining directly with bureaus to set production targets and later profit-sharing agreements for their enterprises and by exploiting information asymmetries to their advantage during these negotiations.<sup>140</sup> Once enterprise heads reached agreements with bureaus, they took on greater responsibility for enterprise operations—from purchasing matters to personnel decisions to strategic planning to employee remuneration schemes—and for the allocation of retained profits. In addition, enterprise heads could shape the structure of their organizations by developing new positions and departments to carry out new tasks—like budget-making, marketing, distribution, and strategic planning—or by

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<sup>139</sup> 陈清泰 [Chen Qingtai]: 《抓住当前深化企业改革的有利时机, 进一步推动企业集团试点工作》 [Seize the Current Opportunity to Deepen Enterprise Reform, Further Promote Enterprise Group Pilot Work] in 《我国企业集团试点的政策与实践》 [China's Enterprise Group Pilots Policies and Practice] (Beijing: Zhongguo jingji chubanshe, 1995): 12.

<sup>140</sup> For one of the few comparative empirical analyses of contract negotiation under the contract responsibility system and enterprise heads' role in their implementation through strategic decision-making, see Chapters 5 and 6 in Derong Chen, *Chinese Firms between Hierarchy and Market: The Contract Management Responsibility System in China* (London: Springer, 1994).

clarifying the roles and responsibilities of existing departments and positions. Government bureaus' declining influence also boosted enterprise heads' authority within their own organizations. As John Child (1996) writes: "Under the new conditions, directors have more opportunities to centralize decisions to themselves, perhaps in the desire to secure a more unified approach, or because they may not trust the capabilities of subordinates, or simply due to the fact that they now bear a more exposed personal responsibility for their enterprise's performance."<sup>141</sup>

However, government bureaus' continued involvement in state-owned enterprise affairs constrained enterprise heads' nascent space for political leadership at the organization level. Bureaus continued to control state-owned enterprises' access to finance, markets, and material inputs, perpetuating state-owned enterprises' dependency on higher administrative authorities despite the formal expansion of enterprise autonomy.<sup>142</sup> In what some colloquially termed "the mother-in-law problem," bureaus also exerted influence over enterprise affairs through their authority to regulate enterprise operations and product quality, grant administrative approvals, and provide what was in effect obligatory guidance on production matters and organizational restructuring. Max H. Boisot (1987) even uses the concept of "industrial feudalism" to suggest that provincial and municipal authorities during the early reform period continued to tightly control state-owned enterprises within their jurisdictions.<sup>143</sup> According to the World Bank Enterprise Surveys conducted between

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<sup>141</sup> John Child, *Management in China During the Age of Reform* (Cambridge: Cambridge University Press, 1996): 87.

<sup>142</sup> Ibid: 26-27.

<sup>143</sup> Max H. Boisot, "Industrial Feudalism and Enterprise Reform: Could the Chinese Use Some More Bureaucracy?" in *Management Reforms in China*, ed. Malcolm Warner (London: Frances Pinter, 1987):

1991 and 1992, only 29% of the state-owned enterprises polled reported having complete autonomy to set their own production plans.<sup>144</sup> Many enterprise heads were reluctant to attempt to shake off bureau influence because government bureaus controlled their salaries and/or had appointed them to their positions.<sup>145</sup>

### ***Establishment of a Socialist Market Economy (1992-1994)***

At the 14<sup>th</sup> Party Congress in October 1992, Jiang Zemin formally set the establishment and refinement of a socialist market economy system (社会主义市场经济, *shehui zhuyi shichang jingji*) as the goal of China's future reform efforts.<sup>146</sup> This concept affirmed that diverse economic components could co-exist (多种经济成分并存, *duo zhong jingji chengfen bingcun*) while upholding the continued dominance of state ownership (公有制为主体, *gongyou zhi wei zhuti*). It was a major breakthrough because it authorized and legitimized initial diversification of state-owned enterprises' ownership rights. It also suggested that state ownership could be embodied in different organizational forms at the firm level, such as wholly state-owned limited liability companies or majority state-owned shareholding companies, and that a single state-owned enterprise might pass through multiple organizational forms during the process of corporatization.

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217-237. See also Max H. Boisot and John Child, "The Iron Law of Fiefs: Bureaucratic Failure and the Problem of Governance in the Chinese Economic Reforms," *Administrative Science Quarterly* 33, no. 4 (1988): 507-527.

<sup>144</sup> Jefferson and Singh 1998: 44.

<sup>145</sup> According to the World Bank Enterprise Survey conducted between 1991 and 1992, 92.8% of the heads of the 889 state-owned enterprises in the sample were appointed by their supervisory agency. Jefferson and Singh 1998: 49.

<sup>146</sup> Jiang Zemin, Report to the National Party Congress, October 12, 1992.

Reform to China's state-owned enterprises during the socialist market economy period aimed to establish a "modern enterprise system" (现代企业制度, *xiandai qiye zhidu*) through shareholding system restructuring (股份制改组, *gufen zhi gaizu*) and separating government from enterprises (政企分开, *zhengqi fenkai*). Initial restrictions on partial public listing of state-owned assets gave way to limited embrace of stock markets as an important means of financing enterprise development and reducing burdens on state-owned banks. Concurrent efforts to separate government from enterprises sought to formalize the separation of ownership and control rights, although government and Party influence on the largest industrial enterprises remained strong.

#### *Shareholding System Restructuring (1992)*

Jiang Zemin's 1992 Report defined the characteristics of a 'modern enterprise system' as: "clearly established property rights, well-defined power and responsibility, separation of enterprise from government, and scientific management."<sup>147</sup> It kicked off a process of shareholding system restructuring (股份制改组, *gufen zhi gaizu*) reform in which state-owned enterprises were to reorganize into limited liability companies or shareholding companies.<sup>148</sup> Unlike earlier shareholding system reforms in which stock was issued primarily to employees and other enterprises, the new reform encouraged

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<sup>147</sup> Ibid.

<sup>148</sup> For an explanation of the differences between limited liability companies and shareholding companies' capital registration requirements, authority structures, and share liquidity, see Lin and Zhu 2001: 310-311.

some state-owned enterprises to publicly issue shares on domestic stock markets.<sup>149</sup>

China's top leaders hoped that shareholding system restructuring would constrain government intervention in state-owned enterprises, improve their market performance, reduce debt burdens by creating a new channel to raise capital, and transform the government's previously unlimited liability into limited liability.<sup>150</sup>

The State Council launched comprehensive enterprise shareholding reform efforts in May 1992 with directives detailing the procedures for enterprises to restructure and issue stock.<sup>151</sup> By the end of 1992, there were nearly 3,700 shareholding system reform pilot enterprises nationwide, including 69 publicly listed enterprises.<sup>152</sup> The number of enterprises publicly listed on the Shanghai and Shenzhen stock exchanges rose steadily, reaching 185 at the end of 1993, 291 at the end of 1994, and 334 at the end of 1995.<sup>153</sup> The State Council also signaled in 1994 that ownership rights for China's largest industrial enterprises would be diversified, when it selected three general corporations under central government ministries to

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<sup>149</sup> Of the 3,800 enterprises that had issued stocks as of 1988, 85% issued stock to their own employees, 13.5% sold stock to other enterprises and 1.5% sold stock to the open market. Naughton 1995: 219. For discussion of early enterprise shareholding reforms, see 王梦奎: [Wang Mengkui], 邢俊芳 [Xing Junfang] 《关于股份制问题》 [On the Issue of Shareholding] (Beijing: Zhongguo jingji chubanshe, 1987).

<sup>150</sup> 彭强 [Peng Qiang]: 《全民所有制企业改组为国家独资有限公司的设想》 [Thoughts on Reorganization of Ownership by the Whole People into Wholly State-owned Limited Liability Companies], 《改革内参》 [Internal Reference Materials on Reform] 13 (1993): 18-19.

<sup>151</sup> State Economic Restructuring Commission, State Economic Commission, Ministry of Finance, People's Bank of China, State Council (Production Office): 《股份制企业试点办法》 [Enterprise Shareholding Pilot Measures], May 11, 1992; State Economic Restructuring Commission: 《股份有限公司规范意见》 [Opinions on Standardizing Shareholding Companies], 《有限责任公司规范意见》 [Opinions on Standardizing Limited Liability Companies], May 11, 1992.

<sup>152</sup> Zhang 2006: 305.

<sup>153</sup> Ibid: 371, 406.

pilot experimental restructuring as state holding companies (国家控股公司, *guojia konggu gongsi*).<sup>154</sup>

However, shareholding reform faced multiple obstacles. State-owned enterprises that publicly issued stock faced a plethora of practical problems, from determining the market value of their assets to securing professional services in China's fledgling accounting and legal sectors. They also faced the risks of mounting speculation and weak government oversight of domestic stock exchanges.<sup>155</sup> Moreover, much shareholding system restructuring occurred in name only: enterprises reported that they had reorganized in order to fulfill reform requirements without actually making any fundamental changes to firm management or operations. Such enterprises became popularly known as turn-card enterprises (翻牌公司, *fanpai gongsi*) for their superficial adoption of new organizational forms. Experimentation with large-scale state holding companies also floundered, as central ministries persisted in using administrative methods to control the pilot enterprises.<sup>156</sup>

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<sup>154</sup> These companies were China Petrochemical Corporation (Sinopec), Aviation Industry Corporation of China (AVIC), and China Nonferrous Metals Industry Group. Zhang 2006: 371, 430.

<sup>155</sup> As senior economist Wu Jinglian wrote: "...In the initial period, accounting firms, law firms and other organizations are not yet sound, rules for stock issuance and circulation are incomplete, supervision and management is not strict, causing China's shareholding reform pilots to fail to achieve the desired results. Not only have they not served their function, on the contrary they have for some time caused a speculative atmosphere in financial markets and the occurrence of an economic "bubble." 吴敬琏 [Wu Jinglian]: 《大中型企业改革: 建立现代企业制度》 [Reform of Large and Medium-sized Enterprises: Establishing a Modern Enterprise System] (Tianjin: Tianjin renmin chubanshe, 1993).

<sup>156</sup> In 1996, the State Council sought to revive lagging reforms by reaffirming the autonomy of the three pilot enterprises' holding companies to manage and delegate authority to their member enterprises; establishing procedures safeguarding their ability to reinvest their operational income without administrative interference; and granting them greater control rights with regard to investment, capital raising, and other matters. Zhang 2006: 430-431.

*Separating Government from Enterprises (1992)*

The separation of government from enterprises (政企分开, *zhengqi fenkai*) was a core element of the ‘modern enterprise system.’ It aimed to formalize the separation of ownership and control rights, by removing enterprise functions from government and curbing administrative interference in enterprise affairs. However, the Chinese leadership did not initially equate this principle with corporate governance (公司治理, *gongsì zhìlǐ*).<sup>157</sup> Neither Jiang Zemin’s 1992 Report nor the 1993 Decisions mentioned corporate governance.<sup>158</sup> Early drafts of the 1993 Decisions originally included corporate governance; however, it was ultimately omitted from the final version due to internal debate.<sup>159</sup> Introducing corporate governance institutions in state-owned enterprises raised the sensitive political issues of personnel selection authority and the relationship between existing Party committees and boards of directors.<sup>160</sup>

Initial efforts to develop a ‘modern enterprise system’ by separating government from enterprises therefore focused on the adoption of new forms of corporate organization, rather than corporate governance. However, the first national pilot scheme to develop a ‘modern enterprise system’ along these lines in 1994 ended

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<sup>157</sup> In an influential 1993 article “On Corporatization,” economists Wu Jinglian and Qian Yingyi had explicitly linked the concepts of a ‘modern enterprise system’ and ‘corporate governance,’ contending that corporate governance constituted the heart of the concept of a ‘modern enterprise system.’ 吴敬琏 [Wu Jinglian], 钱颖一 [Qian Yingyi]: 《关于公司化》 [On Corporatization], 《经济日报》 [The Economic Daily], August 24, 1993.

<sup>158</sup> The Chinese term initially used for corporate governance was “法人治理结构, *faren zhili jiegou*”; later it was commonly referred to as “公司治理制度”, *gongsì zhìlǐ zhìdù*” or “公司制度, *gongsì zhìdù*.” Neither of these terms appeared in the 1993 Third Plenum Decisions.

<sup>159</sup> The same was true of the 1997 15<sup>th</sup> NPC report. Interview with participant in the drafting process, Beijing, June 2017.

<sup>160</sup> For discussion of the Party’s role in ‘modern enterprises’ and specific methods proposed to ensure the Party committee’s continued participation and influence in enterprise decision-making, see Central Organization Department (Party-Building Research Institute), 《党建研究纵横谈》 [Party-Building Research Discussion] (1993): 139-153.



in disappointment.<sup>161</sup> Most of the 100 pilot enterprises reorganized themselves as wholly state-owned enterprise groups (国有独资企业集团, *guoyou duzi qiye jituan*) and kept the “factory system” (工厂制, *gongchang zhi*) method of enterprise governance.<sup>162</sup> An internal review conducted one year later concluded that not a single pilot enterprise met the assessment standards. “It was a change of form but not of substance (换汤不换药, *huan tang bu huan yao*),” recalled a retired official who participated in assessing the pilot enterprises.<sup>163</sup> The State Economic and Trade Commission formally attributed the pilot’s failure to six factors: absence of a central-level system for managing state-owned assets, lack of diversified channels to raise capital, contradictions between the cadre management system and modern enterprise system, limited public listing of state-owned assets, nascent social welfare system, and limited fiscal resources to support the costs of reform.<sup>164</sup>

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<sup>161</sup> Zhu Rongji and other leading officials outlined plans for this pilot scheme at the “National Working Conference for Experiments in Establishing a Modern Enterprise System” in November 1994. Li Peng authorized the State Economic and Trade Commission to lead the pilots. The State System Restructuring Commission was granted a secondary role and allocated authority for 30 of the 100 enterprises selected to participate in it.

<sup>162</sup> The remaining firms restructured as stock companies (股份有限公司, *gufen youxian gongsi*) or limited liability companies (有限责任公司, *youxian zeren gongsi*). State Economic and Trade Commission: 《国有企业改革与建立现代企业制度》 [State-owned Enterprise Reform and Establishing a Modern Enterprise System] (Beijing: Falü chubanshe, 2001): 24.

<sup>163</sup> Interview, Beijing, June 2016.

<sup>164</sup> State Economic and Trade Commission (Enterprise Reform Division): 《国有企业改革与建立现代企业制度》 [State-owned Enterprise Reform and Establishing a Modern Enterprise System] (Beijing: Falü chubanshe, 1999): 31-32. For the State System Restructuring Commission’s assessment, see 邹东涛 [Zou Dongtao], 张晓文 [Zhang Xiaowen]: 《试点企业印证了改革的难度》 [Pilot Enterprises Prove the Difficulty of Reform], 《改革内参》 [Internal Reference Materials on Reform], 24 (1998): 15-17.

### *Creating Space for Political Leadership at the Organization Level*

State-owned enterprise heads' space for political leadership during this period expanded from the operational management of production (生产经营自主权, *shengchan jingying zizhu quan*) to include greater control over the operational management of state-owned assets (资产经营权, *zichan jingying quan*)—their sale, lease, and transfer—and to a limited extent also the operational management of state-owned capital.<sup>165</sup> The 1992 “Regulations on the Transformation of Operational Mechanisms of Industrial Enterprises Owned by the Whole People” issued by the State Council was a milestone: it legally authorized state-owned enterprise heads to exercise decision-making rights across a wide range of 14 areas, including: production, product and labor prices, imports and exports, investments, asset allocation (sale, mortgage and transfer), and joint ventures and mergers.<sup>166</sup>

Newly empowered enterprise heads restructured their firms and formulated specific strategies to realize reform objectives, under rising pressure from official expectations and markets alike. Take for instance Chen Zhongbiao (陈忠表), the general manager of China Ocean Shipping, one of the pilot firms in the development

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<sup>165</sup> See for example the granting of greater asset management autonomy to seven pilot enterprises in 1992. National State Assets Administration Bureau, State Planning Commission, State Council Economic and Trade Office: 《关于国家试点企业集团国有资产授权经营的实施办法（暂行）》 [Temporary Measures for the Implementation of State Enterprise Group Pilots State-owned Assets Operational Authority], September 11, 1992. China Textile Machinery Industry Group [中国纺织机械工业集团] was later added as an eighth pilot enterprise.

<sup>166</sup> State Council: 《全民所有制工业企业转换经营机制条例》 [Regulations on Transformation of the Operational Mechanisms of Industrial Enterprises Owned By the Whole People], July 23, 1992. For a summary of internal debates during the drafting process, see State System Restructuring Commission (Policy and Regulation Division): 《关于制定《全民所有制工业企业转换经营机制暂行条例》内部讨论情况》 [Circumstances of the Internal Discussion about Drafting “Regulations on Transformation of the Operational Mechanisms of Internal Enterprises Owned by the Whole People”, 《内部参考》 [Internal Reference Materials] 7 (1992): 18-24.

of large state-owned enterprise groups. Under Chen's leadership, China Ocean Shipping reduced the holding company's layers of management and cut its original personnel allocation of 700 employees to 300, while also establishing a finance company within the state-owned business group and new member companies in international trade, real estate, and tourism. In 1993, Chen proposed an overseas expansion strategy of "feeding yourself" (自己养活自己, *ziji yanghuo ziji*) that called for the establishment of five new member companies focused on business in Europe, North America, Hong Kong, Japan, and Singapore and the transformation of China Ocean Shipping's existing overseas representative offices into semi-autonomous wholly-owned member companies (联营公司, *lianying gongsi*).<sup>167</sup> As Lisa Keister and Randy Hodson (2009) observed of this period: "Managers were aware that enterprise closures were likely to become more common with time, and many responded by ascertaining firm strengths and adopting appropriate, but limited, innovations."<sup>168</sup>

Enterprise heads' growing space to make choices about organizational strategies and structure was also evidenced by their ability to resist or delay implementing new enterprise reforms. Take for example the appearance of "turn-card" enterprises after 1992. State-owned enterprise heads responded to the center's shareholding system reforms by reporting that their enterprises had restructured as limited liability companies or shareholding companies—without in fact making

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<sup>167</sup> See China Ocean Shipping: 《转换经营机制，大力开展多元化和国际化经营》 [Transforming Operational Mechanisms, Vigorously Carrying Out Operational Diversification and Internationalization] in State Economic and Trade Commission 1995: 103-110.

<sup>168</sup> Lisa A. Keister and Randy Hodson, "Ownership and Innovation During Economic Development: Corporate Ownership and Strategy Formation in China," *Work and Organizations in China After 30 Years of Transition*, ed. Lisa A. Keister (Bingley, UK: Emerald Group Publishing Limited, 2009): 136.

fundamental changes to firm management or operations. While this may have derived in part from lack of knowledge and experience concerning the specific steps that shareholding system restructuring actually entailed, many enterprise heads shied from taking responsibility for the perceived economic and political risks of these novel organizational forms. Instead of a “partial reform equilibrium,” in which those who benefit in the short term attempt to stall continued reform, the initial uncertainty and ambiguity about what the “socialist market economy” concept entailed for state-owned enterprises meant that neither “winners” nor “losers” were immediately clear.<sup>169</sup>

### ***Retrenchment of State Ownership in the “Commanding Heights” (1995-2001)***

Enterprise reforms during this period concentrated state ownership in a core group of large state-owned enterprises in strategically important industries. Far-reaching restructuring of the State Council in 1998 formed a new group of “centrally-controlled enterprises” (中管企业, *zhong guan qiye*). China’s top leaders charged this incipient ‘national team’ with an explicit mandate to help China “catch up” at home and abroad, and they supported them to publicly list assets on domestic and overseas stock exchanges.<sup>170</sup> At the same time, the State Council during the premiership of Zhu Rongji (1998-2003) massively downsized the state-owned economy by allowing

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<sup>169</sup> Joel Hellman, “Winners Take All: The Politics of Partial Reform in Post-Communist Transitions,” *World Politics* 50 (1998): 203-234.

<sup>170</sup> 周明生 [Zhou Mingsheng]: 《资本经营何以雷声大雨点小——杨瑞龙教授访谈录》 [Operational Management of Capital: How The Thunder is Large and the Rain is Small—Record of Interview with Professor Yang Ruilong], 《改革内参》 [Internal Reference Materials on Reform] 8 (1998): 13-15.

thousands of small- and medium-sized state-owned enterprises to be bought up or to go bankrupt.

*Grasping the Large, Releasing the Small (1995)*

The strategy of “grasping the large, releasing the small” (抓大放小, *zhua da fang xiao*) was a critical fork in the road of China’s state-owned enterprise reform.<sup>171</sup> First articulated by Jiang Zemin and Vice Premier Wu Bangguo in 1995, it aimed to consolidate state-owned assets into a select group of larger and more profitable companies that would dominate strategically important industries, while selling off inefficient smaller firms or allowing them to go bankrupt. It envisioned that China’s sprawling state-owned sector would retreat and retrench itself at the ‘commanding heights’ of the economy. Both economic and political considerations motivated this strategy. Proponents contended that ‘key’ state-owned enterprises could be revitalized and strengthened to bolster fiscal stability and promote national development.<sup>172</sup> Retaining and strengthening a small group of ‘key’ enterprises in strategically important industries was also a politically attractive compromise. It ensured that the state would continue to own and control a significant portion of Chinese industry,

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<sup>171</sup> This study focuses on the state’s “grasping” of large enterprises. For an overview of the state’s “releasing” of small enterprises and its social impact, see Xiaobo Hu, “The State, Enterprises, and Society in Post-Deng China: Impact of the New Round of SOE [State-owned Enterprise] Reform,” *Asian Survey* 40, no. 4 (2000): 641-657.

<sup>172</sup> As an internal study group of the State Economic Planning Commission on “The Role of the Government under Market Economy Conditions” observed: “An important motivation for some countries early on to establish state-owned enterprises was to use these enterprises’ profits to guarantee the state’s fiscal revenues.” 周富祥 [Zhou Fuxiang], 石康 [Shi Kang]: 《国有企业不能全面退出竞争性行业》 [State-owned Enterprises Cannot Fully Exit Competitive Industries], 《内部参阅》 [Internal Consultative Readings] 3 (1998): 12.

while allowing the restructuring, privatization, and bankruptcy of smaller and struggling state-owned firms to proceed.

The first task of “grasping the large” was to determine which and how many enterprises to grasp. In 1994, the State Council selected an initial group of 100 large- and medium-size industrial enterprises.<sup>173</sup> In April 1995, Wu Bangguo proposed expanding this to 300 “important enterprises” (重点企业, *zhongdian qiye*), drawn from a larger group of 1,000 “priority enterprises” chosen by the State Economic and Trade Commission earlier that year.<sup>174</sup> In 1997, the State Council expanded the group of “important enterprises” to 512 state firms.<sup>175</sup> This new grouping largely included the previous 100 important large- and medium-size industrial enterprises as well as most of the large enterprise group pilot firms, now numbering 120.<sup>176</sup> The 1998 restructuring of the State Council created a last and critical batch of large state-owned enterprises to join the emerging ‘national team.’<sup>177</sup> It separated 530 large non-financial enterprises from 50 central government agencies; these enterprises were ultimately consolidated into 159 firms, of which 96 were made centrally-controlled

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<sup>173</sup> This group included 28 super-large firms, 67 large firms, and five medium-size firms. Dylan Sutherland, *China's Large Enterprises and the Challenge of Late Industrialisation* (New York: Routledge, 2003): 152.

<sup>174</sup> Of these 1,000 firms, 878 were industrial enterprises. The assets of these 300 firms constituted 46.4% of the total assets of industrial enterprises within the national budget, 52% of their total sales revenue, and 67% of their profits. 吴邦国 [Wu Bangguo]: 《吴邦国同志在全国企业改革试点工作经验交流会上的讲话》 [Speech by Comrade Wu Bangguo at the National Enterprise Reform Pilot Work Experience Sharing Meeting], October 9, 1995, in State Economic and Trade Commission (Enterprise Division): 《建立现代企业制度试点工作手册》 [Establishing a Modern Enterprise System Pilot Work Handbook] (Beijing: Zhongguo jingji chubanshe, 1996): 39.

<sup>175</sup> This grouping of 512 firms was later expanded to 520.

<sup>176</sup> In 1997, the State Council expanded the number of large enterprise group pilot firms from 56 to 120. State Council, State Economic and Trade Commission, State System Restructuring Commission: 《关于深化大型企业集团试点工作的意见》 [Suggestions on Deepening Large Enterprise Group Pilot Work], April 29, 1997.

<sup>177</sup> Restructuring of the State Council reduced the number of ministries from 40 to 29, cut its personnel by one half, and transferred more than 200 government functions to enterprises, social intermediaries, and localities. 《政府工作报告(1999年)》 [Government Work Report (1999)], March 5, 1999.

enterprises.<sup>178</sup> In the process, it took the ‘general corporations’ formed beginning in the 1980s and broke them up into multiple state-owned enterprises along geographic or product/vertical industry lines.<sup>179</sup> Administrative authority for these enterprises was given to the Central Work Committee for Large Enterprises (中央大型企业工作委员会, *zhongyang daxing qiye gongzuo weiyuanhui*).<sup>180</sup>

The second task of “grasping the large” was to designate which sectors constituted the ‘commanding heights’ to which the state should retreat. The sectors represented by the 56 large enterprise group pilot firms in 1991 suggested that these industries were likely to include electricity, defense, basic materials, heavy industry, and airlines.<sup>181</sup> The second batch of 64 large enterprise group pilot firms selected in 1997 roughly doubled the number of enterprises in steel, automobiles, chemicals, and electronics.<sup>182</sup> But the clearest demarcation of the ‘commanding heights’ came in 1999, when the Fourth Plenum adopted a separate policy document stating that state

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<sup>178</sup> These centrally-controlled enterprises included Baosteel, Anshan Steel, China Shipping Group, China Ocean Shipping Group, China Minmetals Corporation, Sinochem, and China State Construction Engineering Corporation. Out of the 159 firms, the remaining 63 enterprises were transferred to provincial governments. Li 2014: 71-72.

<sup>179</sup> For example, the State Council divided the State Electricity Company (of the former Ministry of Electricity) into the State Grid Corporation of China and the China Southern Power Grid Corporation according to asset location along the country’s north-south divide. It split China Nonferrous Metals Industry Corporation (of the former Nonferrous Metals Bureau of the Ministry of Nonferrous Metals) by metals type into China Copper and Lead Group Corporation, China Aluminum Group Corporation, and China Rare Earth Metals Group Corporation. Although these enterprises formally became separate entities, the State Council and its commissions continued to exercise administrative control over them and interfere in their operations, investment, and planning. 刘小玄 [Liu Xiaoxuan], ed., 《中国企业发展报告 1990 ~ 2000 年》 [Report on Chinese Enterprise Development, 1990-2000] (Beijing: Shehui kexue wenxian chubanshe, 2001).

<sup>180</sup> This Committee, together with the State Economic and Trade Commission and the Ministry of Personnel, formed an internal working group to oversee these firms. Central Committee of the Communist Party of China, State Council General Office: 《关于中央党政机关与所办经济实体和管理直属企业脱钩有关问题的通知》 [Notice on Relevant Issues Concerning the Decoupling of Economic Entities and the Management of Directly-Owned Enterprises from Central Party and Government Organs], November 8, 1998.

<sup>181</sup> Sutherland 2003: 50.

<sup>182</sup> Ibid: 50-51.

ownership should maintain the “dominant position” (支配地位, *zhipei diwei*) in “important industries and key areas” (重要行业和关键领域, *zhongyao hangye he guanjian lingyu*). It specified three important industries (sectors relating to national security, natural monopolies, and public goods or services provision) and one key area (high and emerging technology industries)—as well as “backbone enterprises in important industries” (重要产业中的骨干企业, *zhongyao chanye zhong de guban qiye*).<sup>183</sup> This showed top leaders’ commitment to building a team of ‘national champions’: a small group of globally competitive large state-owned enterprises.

*Partial Public Listing of Large Industrial State-owned Enterprise Assets (1997)*

Political support, economic exigency, and international enthusiasm combined to accelerate the partial public listing of large industrial state-owned enterprise assets on domestic and overseas stock exchanges.<sup>184</sup> In March 1999, the State Economic and Trade Commission reported that 30% of 7,680 large and medium state-owned enterprises were operating at a loss and one third of the 512 key large state-owned enterprises made losses during the first half of 1998.<sup>185</sup> Moreover, state-owned companies accounted for an estimated 90% of all non-performing loans held by state-

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<sup>183</sup> Central Committee of the Communist Party of China: 《中共中央关于国有企业改革和发展若干重大问题的决定》 [The Decision of the Central Committee of the Communist Party of China on Major Issues Concerning the Reform and Development of State-Owned Enterprises], September 22, 1999.

<sup>184</sup> The China Securities Regulatory Commission began to review and approve central state-owned companies as listing candidates for overseas IPOs in 1993, with 23 firms approved by December 1996; however, their actual public listing lagged behind because few were attractive candidates for investment. Carl Walter and Fraser Howie, *Red Capitalism: The Fragile Financial Foundation of China's Extraordinary Rise* (New York: John Wiley & Sons, 2012): 177.

<sup>185</sup> China Statistical Yearbook.



owned banks by 1999.<sup>186</sup> During the first half of 1999, Jiang Zemin and Zhu Rongji acted in concert to dispel the looming spectre of economic crisis. Jiang Zemin personally chaired regional meetings across China on state-owned enterprise reform and development in Chengdu, Wuhan, Xi'an, Qingdao, and Liaoning.<sup>187</sup> On June 7, Zhu Rongji held an internal meeting with the heads of 15 major state-owned enterprises and ordered them to “restructure and go to market at any cost” by year’s end. Within days, China National Petroleum Corporation (CNPC) signed a multi-million dollar contract for the largest-ever audit conducted by a foreign auditing company in China, in preparation for public listing of core production and business assets.<sup>188</sup> International investors also played a key role in the restructuring of state-owned assets for public listing.<sup>189</sup> By the end of 2000, CNPC subsidiary PetroChina carried out a dual IPO on the Hong Kong and New York stock markets, and Sinopec completed a triple IPO on the Hong Kong, New York, and London stock markets.

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<sup>186</sup> Ibid.

<sup>187</sup> 《江泽民在成都主持召开四省市国有企业改革和发展座谈会》 [Jiang Zemin Holds a Symposium in Chengdu on Reform and Development of State-owned Enterprises in Four Provinces and Cities], 《人民日报》 [People’s Daily], April 23, 1999; 《江泽民在武汉主持召开六省区国有企业改革和发展座谈会》 [Jiang Zemin Holds a Symposium in Wuhan on Reform and Development of State-owned Enterprises in Six Provinces and Autonomous Regions], 《人民日报》 [People’s Daily], May 31, 1999; 《江泽民主持召开西北五省区国有企业改革和发展座谈会》 [Jiang Zemin Holds a Symposium on the Reform and Development of State-owned Enterprises in Five Provinces and Autonomous Regions in Northwest China], 《人民日报》 [People’s Daily], June 18, 1999; 《江泽民主持召开华东七省市国有企业改革和发展座谈会》 [Jiang Zemin Holds a Symposium on the Reform and Development of State-owned Enterprises in Seven Provinces and Cities in East China], 《人民日报》 [People’s Daily], June 27, 1999; 《江泽民主持八省区市国企改革和发展座谈会》 [Jiang Zemin Holds a Symposium on the Reform and Development of State-owned Enterprises in Eight Provinces and Cities], 《人民日报》 [People’s Daily], August 13, 1999; 《江泽民主持八省区市国企改革和发展座谈会》, 《人民日报》 [People’s Daily], August 13, 1999.

<sup>188</sup> Cable from U.S. Embassy in Beijing, June 1999, declassified (in part) at author’s request on April 6, 2016.

<sup>189</sup> Describing China Mobile’s IPO as “God’s work by Goldman Sachs,” Carl Walter and Fraser Howie write: “International markets introduced Chinese companies to world-class investment bankers, lawyers, and accountants and brought their legal and financial technologies—the entire panoply of corporate finance, legal and accounting concepts, and treatments that underpin international financial markets—to bear on China’s SOE [state-owned enterprise] reform effort.” Walter and Howie 2012: 177.

Other ‘national champions’ followed suit, including: China Unicom (2000), China National Offshore Oil (2001), and Aluminum Corporation of China (2001).<sup>190</sup>

### *Corporate Governance (1999)*

Chinese leaders turned back to corporate governance after organizational restructuring alone failed to transform the performance of the 100 enterprises in the 1994 “modern enterprise system” pilot. The term “corporate governance” appeared in an official document for the first time in 1999. That year, the “Decisions of the Communist Party of China Central Committee on Several Major Issues Concerning the Reform and Development of State-owned Enterprises” mandated that all restructured state-owned enterprises (改制公司, *gaizhi gongsi*) must establish “an effective corporate governance structure” (有效的法人治理结构, *youxiao de faren zhili jiegou*).<sup>191</sup> By the turn of the century, the Chinese government had come to consider corporate governance as an essential component of a ‘modern enterprise system.’<sup>192</sup> However, corporate governance remained a peripheral reform priority for the largest state-owned industrial firms.

Yet despite belated official embrace of corporate governance, early reforms had limited actual impact because they still involved changes in form but not function.

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<sup>190</sup> Walter and Howie 2012: 183.

<sup>191</sup> Central Committee of the Communist Party of China 1999. Corporate governance in China was synonymous with the “new three committees” (新三会, *xin san hui*): the board of directors, the supervisory committee, and the shareholders meeting. The “old three committees” (老三会, *lao san hui*) referred to the Party committee, workers representative assembly, and workers union.

<sup>192</sup> A study by the State Economic and Trade Commission stated: “Only on the basis of standardized corporate governance and genuine transformation of operational mechanisms can a modern enterprise system truly be built and real reform results achieved.” State Economic and Trade Commission 1999: 32-33.

As Zhang Delin (2008) describes this phenomenon: “It was rather like drawing a tiger with a cat as a model; they were not able to fathom the true meaning of the principle and structure of corporate governance—that is, the principle of separation and balance of power—or to adapt it to the enterprises that they were reforming.”<sup>193</sup> Moreover, in most large state-owned enterprise groups, only the publicly listed subsidiaries established boards of directors—not the unlisted holding companies that held their controlling shares and administered the bulk of (unlisted) state-owned assets. In addition, administrative bureaus and government officials at multiple levels continued to routinely intervene in and extract profits from state firms.<sup>194</sup> Boards of directors’ influence on managerial decision-making in state-owned enterprises therefore remained circumscribed in practice.

#### *Creating Space for Political Leadership at the Organization Level*

State-owned enterprise heads’ space for political leadership expanded during this period; however, it did not exhibit uniform growth. Overall, state-owned enterprise heads gained space for political leadership because of the green light given to “strategic restructuring” of the state-owned economy and of individual firms within it. While the massive downsizing of the state sector under Zhu Rongji was a central-level strategy, much of the decision-making that drove it occurred at the firm level, as individual enterprises and their heads decided how many employees to lay off and

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<sup>193</sup> Zhang Delin, “Reform of State-owned Enterprises: A Three Year Disconnect from Difficulties Leads to System Innovation,” *China in the Wake of Asia’s Financial Crisis*, ed., Wang Mengkui (New York: Routledge, 2008): 147.

<sup>194</sup> Edward S. Steinfeld, *Forging Reform in China: The Fate of State-owned Industry* (New York: Cambridge University Press, 1998).

when, which assets to lease or sell, or which firms to acquire. Under state supervision, enterprise heads were permitted to select part of their enterprises' assets and apply for public listing in order to access new sources of capital; they then had considerable latitude to determine how to invest this capital in equipment and technology upgrading or in other areas. State-owned enterprises at all levels pushed for expanded rights to manage capital (资本经营, *ziben jingying*) despite practical constraints.<sup>195</sup> Finally, some enterprises and their managers formalized and expanded their control rights vis-à-vis the state through corporate governance development.

In addition, the State Council encouraged enterprise heads to take responsibility for formulating the specific strategies for their firms' development and restructuring. In a 1995 speech, Wu Bangguo explained: "This development strategy should be realistic, accurately identifying one's own position in both domestic and international markets, getting clear about one's advantages—a realistic development strategy is particularly important for enterprise groups. It must solve internal stock adjustment, enabling resources to flow in the direction of development and good efficiency."<sup>196</sup> Enterprise leaders now navigated between the state and markets to chart a comprehensive, long-term development path for their organizations, moving beyond the bargaining relationship with bureaus and the short-term responses to market pressures that had characterized the earlier reform period.

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<sup>195</sup> Zhou 1998: 13-15.

<sup>196</sup> 吴邦国 [Wu Bangguo]: 《吴邦国同志在与参加国家试点企业集团工作会议代表座谈时的讲话》 [Speech by Comrade Wu Bangguo to Representatives Attending the Work Meeting on Enterprise Group National Pilots] in State Economic and Trade Commission (Enterprise Division): 《我国企业集团试点的政策与实践》 [China's Enterprise Group Pilots' Policies and Practice] (Beijing: Zhongguo jingji chubanshe, 1995): 5.

However, the space for political leadership did not expand unequivocally for the heads of the largest industrial enterprises. On the one hand, these individuals gained greater autonomy within the overall administrative hierarchy. The 1998 State Council restructuring abolished the State Assets Administration Bureau (国有资产管理局, *guoyou zichan guanli ju*), the central-level government body previously responsible for overseeing state-owned assets.<sup>197</sup> The State Council restructuring also formally cut some state-owned enterprises loose from the central ministries in which they had been embedded. In addition, the domains over which enterprise heads could exercise political leadership increased in tandem with the growing size and scope of state-owned business groups. On the other hand, the lack of a single central-level organization responsible for state-owned enterprise oversight and reform ushered in the “five dragons ruling the waters” (五龙治水, *wu long zhi shui*) period, in which multiple government and Party organizations charged with various responsibilities for state-owned enterprise affairs continued to interfere in their operations.

Moreover, some state-owned enterprise heads struggled to exercise political leadership at the organization level even though they possessed greater space to do so. A classified report in 1999 about a World Bank training project in China observed that Chinese state-owned company managers found it difficult to delegate authority, to make strategic rather than tactical decisions, and to use inductive reasoning to flexibly respond to rapidly changing market conditions.<sup>198</sup> The report cited obstacles including

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<sup>197</sup> The State Assets Administration Bureau was set up in 1988 under the Ministry of Finance. Similar agencies were established earlier at provincial and municipal levels.

<sup>198</sup> The report attributed this to state-owned company managers’ education and practices during the command economy era, in which they strictly employed standard operating procedures, hierarchical

state-owned enterprise leaders' fear of losing their authority and the resources for patronage it conferred, as well as the perceived risk of being held accountable for decisions delegated to subordinates. "SOEs [state-owned enterprises] need managers able to provide strategic leadership on market-oriented production in a changing environment, while delegating operational decision-making authority to subordinates," the report stated, concluding that state-owned company managers "need a fundamental change in their belief and cognitive systems."<sup>199</sup> In summary, the World Bank report underscores the point that enterprise heads did not always act to exercise political leadership through proactive choices about organizational strategy and structure, even if they enjoyed greater autonomy to do so.

### ***Internationalization and Consolidation of the State Sector (2002 On)***

Deepening of two interrelated trends distinguish post-2002 developments. The first trend is the internationalization of state-owned enterprises' operations, assets, and capital. The 16<sup>th</sup> National Party Congress in November 2002 formalized a "going out policy" as a major measure marking a new official stage of China's reform and opening movement. Under the auspices of this policy, the Chinese government has provided firms—especially state-owned enterprises—with a wide range of economic, political, and administrative support to pursue overseas expansion. The second trend is the consolidation of state-owned assets and authority for their administration. The Hu Jintao administration's creation of the State-owned Assets Supervision and

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chains of command, and deductive reasoning to respond to central plan directives and expected performance criteria. U.S. Department of State Cable from Shenyang Consulate, February 1999, declassified (in part) at the author's request on March 30, 2016.

<sup>199</sup> Ibid.

Administration Commission (SASAC) in 2003 consolidated central authority, because it ended the “five dragons ruling the waters” period during which authority for administering state-owned assets was fragmented among multiple government and Party agencies.<sup>200</sup> It also created the possibility for further consolidation of state-owned assets, through government-directed mergers of the central state-owned enterprises under SASAC’s administration.

*“Going Out” (2002)*

The 16<sup>th</sup> National Party Congress in November 2002 announced the policy of “going out” (走出去, *zou chuqu*) as a “major measure taken in a new stage of China’s reform and opening movement.”<sup>201</sup> Top Chinese leaders had proposed an economic strategy of “going out” as early as 1998 for a small group of high-performing state-owned enterprises, encouraging them to set up factories in Africa, Central Asia, the Middle East, Eastern Europe, and Latin America.<sup>202</sup> However, formal adoption of the “going out” policy in 2002 differed from these early statements because it proposed a comprehensive, long-term global expansion strategy outlining a fundamental shift in economic orientation—from the internationalizing domestic economy toward world markets—for all Chinese enterprises. It marked a new phase in enterprise reform in which the state actively encouraged enterprises to engage in non-financial and financial overseas direct investment, cross-border mergers and acquisitions, joint

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<sup>200</sup> This study focuses on the central-level SASAC, created as a special agency of the State Council to represent the state’s ownership rights and administer a portfolio of central state-owned enterprises. SASAC was originally given responsibility for administering 196 central state-owned enterprises; however, their number shrank to 189 due to restructuring by the time SASAC began operations in 2003.

<sup>201</sup> Jiang Zemin, Report to the National Party Congress, November 8, 2002.

<sup>202</sup> Jiang Zemin: 《做好国内经济工作，增强承受和抵御风险的能力》 [Doing Domestic Economic Work Well, Strengthening the Ability to Withstand and Resist Risks], February 26, 1998.

ventures overseas with foreign firms, and establishment of foreign affiliates (subsidiary companies registered overseas) through measures from targeted loans to liberalization of regulations and administrative rules.<sup>203</sup>

The “going out” policy has catalyzed ongoing growth in Chinese enterprises’ investments, revenues, assets, and numbers of employees abroad. Between 2002 and 2015, China’s non-financial outward direct investment grew at an average annual rate of 33.6%.<sup>204</sup> In 2015, China became a net capital exporter when its enterprises’ total overseas direct investment surpassed total foreign direct investment for the first time.<sup>205</sup> China’s central state-owned enterprises now operate in 185 countries and regions worldwide, with total overseas assets of \$725.6 billion and 346,000 employees abroad.<sup>206</sup> At the organization level, the “going out” policy has impelled the heads of large state-owned enterprises to develop strategies specifically targeting overseas expansion and to adapt their organizational structures at home (for example, by reorganizing headquarters departments originally set up along product lines into departments organized by geographic region) and abroad (for example, by establishing new offices abroad to manage existing operations and develop future business).

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<sup>203</sup> The state’s previous efforts to liberalize and foster cross-border economic activities had primarily involved foreign direct investment into China, domestic joint ventures and joint research and development initiatives between foreign and Chinese firms, public listing of Chinese enterprise assets on stock exchanges in China and abroad, and support for Chinese firms’ exports.

<sup>204</sup> Ministry of Commerce: “Official of the Department of Outward Investment and Economic Cooperation of the Ministry of Commerce Comments on China’s Outward Investment and Economic Cooperation in 2015,” January 18, 2016. Accessed on August 1, 2017 at: <http://english.mofcom.gov.cn/article/newsrelease/policyreleasing/201602/20160201251488.shtml>.

<sup>205</sup> “China Now a Net Capital Exporter,” *Xinhua News*, January 21, 2015.

<sup>206</sup> Yunbi Zhang, “Nation Will Fine-Tune SOE [State-owned Enterprise] Management Abroad,” *China Daily*, March 22, 2017.



*Creation of SASAC and Central State-owned Enterprises (2003)*

The establishment of SASAC and its portfolio of central state-owned enterprises in 2003 vested authority for the administration of state-owned assets in a powerful new government body.<sup>207</sup> SASAC was granted full ministerial rank and a relatively large personnel allocation of 555 staff.<sup>208</sup> Its mandate to “manage assets, people, and affairs” (管资产, 管人, 管事, *guan zichan, guan ren, guan shi*) gave it significant formal authority over individual enterprises, even though it was not authorized to intervene in their daily operations. SASAC’s establishment also created a new type of state firm: central state-owned enterprises (中央国有企业, *zhongyang guoyou qiye*, commonly abbreviated as 央企, *yangqi*). They included both the former ‘general companies’ set up under central ministry headquarters and later broken up by the 1998 State Council restructuring, as well as the former large enterprise group pilots that originated from lower levels of the former ministry-coordinated production system. Of these central state-owned enterprises, 55 were initially designated core ‘important backbone’ (重要骨干, *zhongyao guban*) enterprises and accorded the equivalent of vice-ministerial rank; the Central Organization Department appointed their heads and they were termed “enterprises managed directly by the center” (直管企业, *zhiguan qiye*).<sup>209</sup> Although both the core and non-core central state-owned enterprises operated

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<sup>207</sup> The 1998 State Council restructuring had abolished the State Assets Administration Bureau, the central-level agency previously responsible for administering state-owned assets, prompting a plethora of organizations to assume responsibility for various aspects of state-owned enterprise affairs.

<sup>208</sup> Kjeld Erik Brødsgaard, “Politics and Business Group Formation in China: The Party in Control?” *The China Quarterly* 211 (2012): 630.

<sup>209</sup> These top leadership positions are the Party committee secretary (党委书记, *dangwei shuji*), general manager (总经理, *zongjingli*), and chair of the board of directors (董事长, *dongshizhang*), if one exists. The remaining central state-owned enterprises were granted the equivalent of department-level rank.

in a range of sectors, the core enterprises were concentrated in industries including defense, energy, airlines, and telecommunications, while the non-core enterprises included numerous independent research and design institutes.<sup>210</sup> Finally, SASAC's establishment created the possibility for government-directed asset consolidation (资产整合, *zichan zhenghe*). The number of SASAC-administered central state-owned enterprises has decreased from 189 in 2003 to 101 and continues to fall; most firms that 'disappeared' were merged into (并入, *bingru*) existing central state-owned enterprises.<sup>211</sup>

### *Creating Space for Political Leadership at the Organization Level*

The directors of the State-owned Assets Supervision and Administration Commission (SASAC) emerged as an important new group of organizational leaders in the state-owned economy upon SASAC's creation in 2003.<sup>212</sup> Because SASAC was set up to serve as a government ownership agency, not merely an administrative department charged with managing state-owned assets (like the former State Assets Administration Bureau), its leaders became central actors in the state's exercise of

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SASAC appointed their heads in consultation with the Central Organization Department and they were considered enterprises whose management was entrusted (托管企业, *tuoguan qiye*) to SASAC.

<sup>210</sup> These independent research and design institutes included: 煤炭科学研究总院 [Coal Science Research Institute], 机械科学研究院 [Institute of Mechanical Science and Technology], 钢铁研究总院 [China Iron and Steel Research Institute], 冶金自动化研究设计院 [Institute of Metallurgical Automation Research], 中国建筑材料科学研究院 [China Building Materials Science Institute], 电信科学技术研究院 [Telecommunications Science and Technology Research Institute], 中国医疗卫生器材进出口公司 [China Medical and Health Equipment Import and Export Corporation], and 中国建筑 designs 研究院 [China Architectural Design and Research Institute].

<sup>211</sup> The number of central state-owned enterprises administered by SASAC was 101 as of July 2017.

<sup>212</sup> This study focuses on the directors of SASAC (国资委主任, *guoziwei zhuren*) rather than the Party Secretaries of SASAC (国资委党委书记, *guoziwei dangwei shuji*), because they possess primary decision-making authority for the organization's affairs.

ownership as well as control rights. SASAC's full ministerial rank and relatively large personnel allocation reflected the authority vested in it and its directors to guide future state-owned enterprise reform experimentation and implementation—indeed, it was given this rank and personnel resources precisely so that it would be able to do this. SASAC's newness as an organization gave its heads considerable latitude to design and alter its organizational structure. They also had significant autonomy to determine the specific strategies that SASAC took to achieve its objectives: preserving and increasing the value of state assets, making central state-owned enterprises internationally competitive, and promoting the development of a modern enterprise system.

However, SASAC and its directors do not operate in a vacuum; they also interface with other organizations regarding state-owned enterprise reform. First, SASAC directors interact regularly with top State Council leaders, in particular the Vice Premier responsible for overseeing state-owned enterprise reform. The Central Organization Department (COD) also exerts important influence on state-owned enterprise reform, particularly in the domains of company governance and Party-building within state-owned enterprises. The COD's authority to either directly select or to advise on the selection of the heads of central state-owned enterprises constitutes another mechanism of its influence.<sup>213</sup> Since 2003, the COD has moved beyond exercising influence through personnel control to weighing in on other matters, in particular corporate governance and the designation of different levels of industry strategic importance. Finally, the Central Committee for Discipline and Inspection

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<sup>213</sup> Chen Li, "Holding 'China Inc.' Together: The CCP and The Rise of China's *Yangqi*," *The China Quarterly* 228 (2016): 927-949.

(CCDI) has emerged as a player in state-owned enterprise affairs with the launch of the Xi Jinping administration's ongoing anti-corruption campaign. These organizations' engagement in matters related to state-owned enterprise reform does not formally reduce SASAC directors' space for political leadership; however, they are other actors that SASAC heads must navigate around or bargain with during reform policy experimentation and implementation.

The heads of central state-owned enterprises are enjoying perhaps their greatest space for political leadership during the reform era. Like SASAC directors, they possess significant autonomy to determine specific strategies to achieve central reform goals—preserving and increasing the value of state-owned assets and building globally-competitive national champions—and to restructure their enterprises in order to do so. The geographic orientation and scope of central state-owned enterprise heads' political leadership has also expanded dramatically. As a growing proportion of revenue for many central state-owned enterprises now comes from international rather than domestic markets, overseas expansion is becoming a more important factor in their heads' strategies and in how they structure their firms. Finally, central state-owned enterprise heads' vice-ministerial or department-level rank provides additional impetus for them to act as political leaders rather than merely as administrative managers. Włodzimierz Brus and Kazimierz Laski (1991) argue that state-owned enterprise heads can never act as more than managers because they do not have the “material foundation of responsibility” for enterprise performance.<sup>214</sup> However, it can be argued that central state-owned enterprise heads do possess a “political foundation

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<sup>214</sup> Włodzimierz Brus and Kazimierz Laski, *From Marx to the Market: Socialism in Search of an Economic System* (New York: Oxford University Press, 1991): 138.

of responsibility,” because they have the possibility for political promotion both within and beyond state-owned industry. The political consequences for central state-owned enterprise heads’ performance—and especially the prospect of political gain—are an additional incentive for them to engage in political leadership rather than simply administrative activities.

Four main factors contributed to the expansion of central state-owned enterprise heads’ space for political leadership during the present phase. The first is the relative reduction of state interference in individual enterprise affairs. Despite SASAC’s ministerial rank and relatively large personnel allocation, it lacks the capacity to manage or even to effectively monitor central state-owned enterprises at the organization level. Each central state-owned enterprise is itself typically a large enterprise group comprising myriad legal entities. SASAC relies primarily on personnel appointment, administrative directives, information reporting, and periodic on-site inspections by its supervisory board; however, these are indirect and incomplete methods of control. Second, steady overall growth in central state-owned enterprises’ size (assets) and revenues since 2003 has boosted their economic and political influence—and that of their heads. Third, the average leadership tenures of central state-owned enterprise heads have lengthened since 2003, as have the numbers of years they worked previously in their firms. Leadership tenures in the core central state-owned enterprises lengthened from an average of 3.9 years for top leaders serving in 2003 to 5.5 years in 2012, while work experience in one’s firm rose from an

average of 7.6 years for top leaders serving in 2003 to 13.1 years in 2012.<sup>215</sup> These trends have contributed to a phenomenon of central state-owned enterprises becoming like small kingdoms, in which the “number-one leader” (一把手, *yi ba shou*) exerts predominant influence on organizational strategies and structure. Fourth, ties to powerful political elites have also expanded space for political leadership for a select few central state-owned enterprise leaders.<sup>216</sup>

## ***Conclusion***

Enterprise reform policies since 1978 have created and increased space for state-owned enterprise heads and SASAC directors to exercise political leadership at the organization level. During the period of ‘dual track’ economic reform, state-owned enterprise heads gained new space to not only manage production but also to influence reform policy experimentation and implementation. They could negotiate with bureaus on the specific targets for their enterprises, determine the specific means by which to achieve them, and reshape their organizations to carry out new tasks like budget-making, strategic planning, and marketing and distribution. However, bureaus’ continued involvement in enterprise affairs—together with their control over access to finance, markets, and material inputs—constrained nascent space for political leadership at the organization level.

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<sup>215</sup> Here I define leadership tenure as the total number of years that an individual serves in one or more of the top three leadership roles at a particular core central state-owned company: Party committee secretary, general manager, and chair of the board of directors, if one exists. It includes both joint appointments (in which a single individual held one or more top leadership roles simultaneously) and consecutive top leadership roles (if a single individual served consecutively in different top leadership roles or combinations of those roles). Wendy Leutert, “The Political Mobility of China’s Central State-owned Enterprise Leaders,” *The China Quarterly* (forthcoming).

<sup>216</sup> Such cases include well-known examples like Zhou Yongkang (周永康), the former head of China National Petroleum Corporation.

After the establishment of a “socialist market economy” in 1992, enterprise heads’ greater autonomy over production matters expanded to encompass the management of both state-owned assets and state-owned capital. Their space for political leadership grew as they took up new responsibilities for restructuring their organizations as limited liability companies or shareholding companies, and formulating development strategies for domestic and in some cases even international markets. Enterprise heads’ growing influence was evident not only in their efforts to implement new enterprise reforms, but in some cases also in their attempts to resist or delay them. The emergence of “turn-card” enterprises after 1992, for example, underscores the growing space for political leadership at the organization level.

With the retrenchment of state ownership in the ‘commanding heights’ of the economy beginning in 1995, enterprise heads gained more space to exercise political leadership by determining specifically how to reform and restructure their organizations. This was particularly true for heads of small and medium state-owned enterprises which survived Premier Zhu Rongji’s overhaul of the state sector. This was also true for large state-owned enterprise groups. The State Council could move them in and out of national pilots and groupings of “important enterprises,” and in some cases even combine them at will—as it did for some in the 1998 State Council restructuring. However, their heads—not the State Council—were responsible for altering their organizational structures as they expanded across regions and incorporated smaller local firms. Heads of large state-owned enterprise groups also formulated their strategies for expansion in domestic and international markets. However, government agencies’ interference in enterprise affairs persisted, especially

after the 1998 State Council restructuring gave a plethora of state agencies responsibility for various aspects of state-owned enterprise affairs.

Since 2003, the directors of SASAC have emerged as an important new group of organizational leaders. These individuals exercise political leadership by determining the specific strategies to achieve the center's goals for the state-owned economy, and by altering the organizational structure of the central state-owned enterprises under SASAC's administration. However, other government and Party bodies' participation in state-owned enterprise affairs constrains SASAC directors' space for political leadership on matters such as personnel appointment. In contrast, heads of the largest state firms have enjoyed their greatest space yet for political leadership during the reform era. This is due primarily to central state-owned enterprises' growing size and global operations, overall reduction in state interference in their affairs, and core central state-owned enterprise heads' lengthening leadership tenures and years of work in their firms. Table 2.2 below summarizes the changing space for political leadership in China's state-owned economy since 1978.



Table 2.2: Space for Political Leadership in China's State-owned Economy Since 1978

| <b>Period</b>  | <b>Space for political leadership at the organization level</b>   |
|--|---|
| <b>Emergence and decline of 'dual track' economic reform (1978-1991)</b>       | State-owned enterprise heads acquire new space to not only manage production but also to influence policy experimentation and implementation  |
| <b>Establishment of a socialist market economy (1992-1994)</b>                 | State-owned enterprise heads' space for political leadership grows as they take up new responsibilities for carrying out organizational restructuring and formulating development strategies  |
| <b>Retrenchment of state ownership in the "commanding heights" (1995-2001)</b> | State-owned enterprise heads' scope for influence expands further to encompass both state-owned capital and state-owned assets; its orientation becomes increasingly international  |
| <b>Internationalization and consolidation of the state sector (2002 on)</b>    | <p>Heads of the largest state-owned enterprises gain their greatest space yet for political leadership due to: enterprises' growing size and global operations, reduction in state interference, and their lengthening enterprise and leadership tenures</p> <p>SASAC heads exercise political leadership by determining specific strategies to achieve the center's goals for the state-owned economy, and by altering the organizational structure of the enterprises under its administration; however, other government and Party bodies constrain their space for political leadership</p> |

## Chapter 3

### **Economic Reform through Political Leadership in a Central State-owned Enterprise**

From the outside, the headquarters of China Building Company in southwest Beijing looks just like that of any other Chinese multinational corporation.<sup>217</sup> Two glass and steel office buildings tower above the adjacent restaurants, shops, and low-rise brick apartment buildings. Security guards monitor the flow of vehicles and people through automatic gates as they enter the office compound. Two flagpoles flying the company and national flags frame the entrance, while a long line of expensive foreign cars—Audis, Mercedes, and the occasional Maserati—wait for executives and visiting senior dignitaries. Once through a glass revolving door, more security guards and reception staff dot a massive marble lobby featuring outsized works of art—carved jade, sculptures, and paintings. A throng of employees fills the lobby at the start of the workday; they stand watching news and commercials on TV screens while waiting for one of the three elevators to arrive. After exiting the elevator on the appropriate floor, employees walk to their departments past flickering electronic signboards displaying company and national news and other information.

Employees begin their workday by changing into the work uniform that is mandatory for most: a navy blue business suit with a collared shirt and formal shoes. Some also wear a gold lapel pin featuring the China Building Company logo. Many arrive before the official start of the workday at 8:30 AM to eat breakfast in the

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<sup>217</sup> The company and individual names used in this chapter are pseudonyms to protect the anonymity of study participants. See Appendix A for a detailed discussion of the case study research design and data.

company cafeteria and prepare tea or coffee. They work in large open rooms scattered with potted plants, in cubicles just tall enough to look over while sitting. Glassed-in offices for department heads border the corners of the rooms. Each desk has its own company-issued computer and telephone, but each department shares a single printer. Employees make phone calls with overseas clients in English, French, and Spanish to discuss projects, while others use the Chinese software program QQ to chat with colleagues about internal approvals for an upcoming tender. There are almost always several desks empty in each office, as staff travel for business in China or overseas, for days or even weeks at a time.

At 10 AM—and again later in the day at 3 PM—several minutes of calisthenics set to brass band music blares automatically through the company’s loudspeakers. Most employees ignore it, although a few go out to the hallway for some light exercise and stretching. Before the cafeteria opens for lunch at 11:30 AM, employees take the stairs down early to line up, past scattered cigarette butts and a lingering odor of smoke that silently mock the “no smoking” signs. In the cafeteria, employees eat buffet-style meals together from metal trays amid loud television news. After lunch it is time for “mid-day rest.” Employees return to the department, turn off the lights, and nap with their heads down on their desks; some even recline fully on company-issued folding cots. Lights are switched back on around 1 PM, and it is back to work. Around 4:50 PM, those with newborn or young children are already trickling out of the office. At 5 PM, the workday formally ends. By 6 PM, only the company leadership, ambitious junior employees keen to rise through the ranks, and a handful of employees living in on-site company housing remain.

These glimpses of the workplace at China Building Company hardly appear to match a strategic design perspective's claim that top national leaders shape the reform process. Top national leaders and their policies are certainly present here—excerpts from an important new speech by Xi Jinping appear on electronic signboards in the corridors, and the Party Committee Work Affairs Department regularly convenes Party members to study national leaders' speeches and central government policies. But political propaganda and education do not equate with control of organizational or individual behavior. While office bookshelves bristle with yellow-bound volumes of Xi Jinping's speeches and writing, employees' personal book collections show greater diversity; works in one desktop collection span Karl Marx's *Capital*, Hillary Clinton's *Living History*, and Francis Fukuyama's *The End of History and the Last Man*. To be sure, the center sets the goals that state-owned enterprises must achieve, the most important of which are: 1.) preserving and increasing the value of state assets; and 2.) becoming internationally competitive firms. Through the cadre management system, the center seeks to incentivize state-owned enterprise heads by linking their political promotion with achievement of these goals. Incentives and constraints imposed by the center are real, but they are not determinative.

Daily work life in China Building Company also underscores the reality that economic reform and globalization are increasingly intertwined. The operations of Chinese state-owned enterprises and the changes that their heads make to organizational strategies and structures now involve personnel, assets, and capital around the world—and they can profoundly affect the local communities and environments in the countries where they operate. Enterprises heads must pay as much

attention to their company's position in international markets as they do to the latest official documents (公文, *gongwen*) from SASAC. Their speeches blend the policy buzzwords of top national and SASAC leadership with discussions of the latest Fortune Global 500 rankings and warnings about possible political turmoil and trade protectionism overseas. Preserving and increasing the value of state-owned assets for many central state-owned companies now hinges on their leaders' abilities to expand business beyond China's borders in Asia, Africa, Latin America, the Middle East, North America, and Europe. A strategic design perspective's focus on policy-making, institutional design, and political competition in Beijing downplays the increasingly global context—and content—of economic reform.

However, this is not to say that economic reform is a process of bottom-up, organic transformation. Central state-owned enterprise heads do not possess authority to make major changes to their companies' organizational structure or operations, such as mergers with other central state-owned enterprises, large-scale layoffs, appointment of top company leadership positions, or establishment of board of directors. Within China Building Company, vertical responsibility and authority relationships shape company operations and individual employees' behavior alike. Vertical responsibility relationships are embodied in the sub-contracting relationships that knit the various layers of the enterprise together from the top down. China Building Company receives annual targets from SASAC and apportions them to its member companies, which in turn allocate them down to individual employees. Vertical authority relationships are evident in myriad ways, from the print-outs of the chairman's annual work plan on employees' desks, to the dense telephone trees showing department and staff

hierarchies pinned to their cubicles, to the supervisor approvals requisite for company matters large and small. Both China Building Company's leadership and its employees operate within distinct hierarchical domains of authority.

In this chapter, I argue that political leadership at the organization level is a critical factor shaping central state-owned enterprises' economic reform. Enterprise heads possess bounded autonomy to determine the specific strategies by which to respond to the center's two main objectives for economic reform of central state-owned enterprises: preserving and increasing the value of state assets and becoming internationally competitive firms. They also have bounded autonomy to alter organizational structure: changing existing authority relations; creating, modifying or abolishing intra-company entities; and reallocating assets, personnel and capital.

Enterprise heads' exercise of political leadership impacts central state-owned enterprises' economic reform, defined as an increase in the level of marketization of their global expansion efforts, expansion in the influence of market-oriented actors relative to that of administrative actors within the firm, and how these intra-firm entities conceptualize their relationship to international markets. Global expansion efforts refer to how intra-firm entities plan, enter, and act in markets outside of China. Broadly speaking, these efforts may be either market-oriented (decentralized) or administrative (centralized). I focus on global expansion efforts because many central state-owned enterprises' overseas business constitutes a significant percentage of their revenues; in some cases, it has already exceeded earnings from the domestic

market.<sup>218</sup> Particularly for central state-owned enterprises in industries suffering from overcapacity or slowing domestic growth, markets abroad are their primary target. Expansion in the influence of market-oriented actors within the firm relative to that of administrative actors reflects the extent to which market-oriented actors can act autonomously at a given time. Finally, I examine whether intra-firm entities' conceptualization of their relationship to international markets is market-oriented or administrative in nature. This is an important measure of economic reform because it reflects both their interpretations of their environment as well as ideas about how it should be ordered. I select these three indicators because they capture important aspects of the process of economic reform and data was available to assess them.<sup>219</sup>

### ***Origins, Organizational Structure, and Key Intra-firm Entities of China Building Company***

SASAC formed China Building Company in 2011 by merging two existing central state-owned companies: Sino-Construction and Sino-Engineering (see Figure 3.1). The merger had two main objectives. Its first objective was vertical industry integration. This was to be achieved by combining Sino-Construction's construction capacity with Sino-Engineering's engineering expertise to create a single, vertically-integrated industry conglomerate. Its second and related objective was to build a global industry leader through this vertical integration and by increasing the new

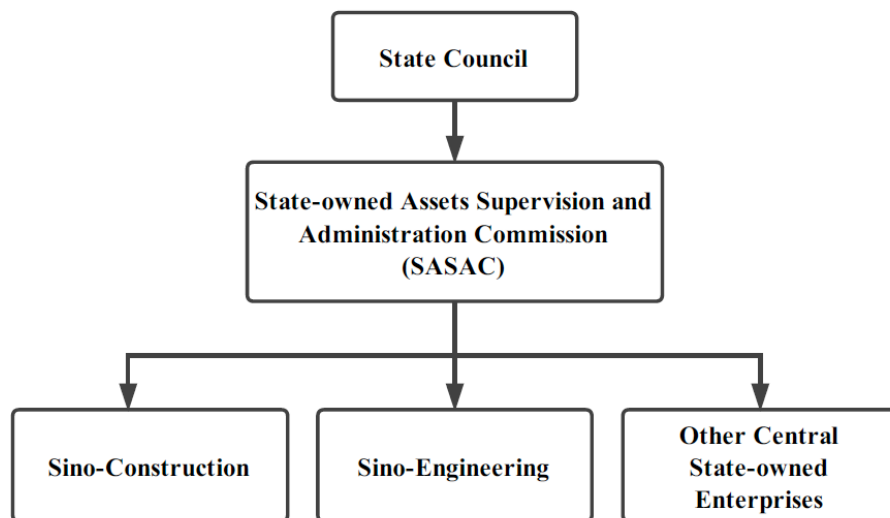
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<sup>218</sup> This was the case for China Building Company: the value of contracts for its overseas projects exceeded the value of its domestic contracts in 2012. *China Building Company Yearbook: 2012-2014* (Beijing, 2015).

<sup>219</sup> There are other indicators of economic reform at the company level beyond the three I study here, such as changes in the specific proportion of the company's assets that were publicly listed on the stock market or variation in the relative amounts and types of state support that it received (for example, preferential financing from state-owned policy banks); however, I did not have access to such data.

company's size and resources: assets, capital, employees, and client networks.<sup>220</sup> Last but not least, the merger also aimed to boost the company's international profile. As an employee working in China Building Company's holding company explained: "If you put the similar state-owned assets together then you will have ... a brand, a name with international recognition."<sup>221</sup>

Figure 3.1: Organizational Structure Before Creation of China Building Company

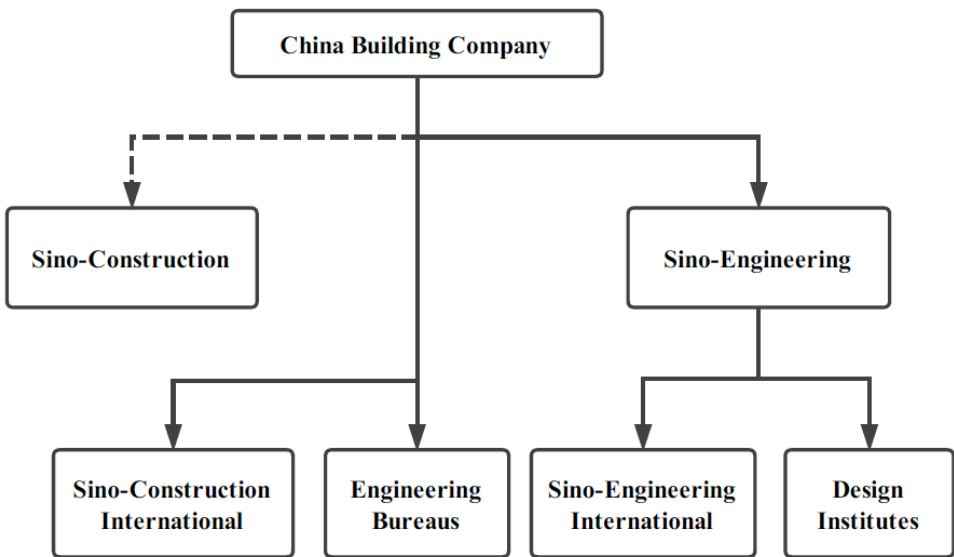


<sup>220</sup> These two objectives are common for government-directed mergers of central state-owned companies in China. Recent similar examples include the merger of China Power Investment Corporation with State Nuclear Power Technology Corporation (2015) and the merger of China North Rail (CNR) Corporation Limited with China South Rail (CSR) Corporation Limited (2014).

<sup>221</sup> Sino-Construction International department employee, Beijing, October 2014.



Figure 3.2: Post-Merger Organizational Structure of China Building Company, During Mr. Chen’s Chairmanship



\* *Sino-Construction was retained in name only after the merger.*

*China Building Company (Holding Company)*

China Building Company, the holding company for the state-owned business group of the same name, functioned primarily as an administrative overseer.<sup>222</sup> The holding company had five main functions: leading, control, service, assessment, and rewards and discipline.<sup>223</sup> It supervised member companies’ management and commercial operations through administrative methods (for example, requiring approvals for company and commercial matters) and personnel (for example, dispatching holding company employees to be based in overseas offices).

<sup>222</sup> China Building Company employees emphasized that the holding company was a purely administrative organization, not a commercial one engaged in business operations. China Building Company employee, Beijing, October 2014.

<sup>223</sup> In Chinese: leading (引领, *yinling*), control (管控, *guankong*), assessment (评价, *pingjia*), service (服务, *fuwu*), and rewards and discipline (奖惩, *jiangcheng*).

### *Sino-Construction International*

Sino-Construction established Sino-Construction International in 2004 as a marketing, investment, and management platform for overseas business. From initial projects and overseas offices in Asia—in Nepal, Malaysia, and Pakistan—Sino-Construction International expanded rapidly into Africa, the Middle East, Latin America, and Europe. From 18 offices in 17 countries in 2004, it expanded to 113 offices in 85 countries by the end of 2014. It increased overseas contracts from nearly 50 signed in 2004 to more than 500 signed in 2015.<sup>224</sup> Its business lines included clean energy plants, large-scale transportation projects, and municipal works like stadiums and water treatment facilities.

### *Engineering Bureaus*

China Building Company had 16 engineering bureaus with offices across China.<sup>225</sup> The engineering bureaus did the actual project construction. Before China Building Company's establishment in 2011, the engineering bureaus were subsidiaries of Sino-Construction International; post-merger, they became subsidiaries of China Building Company with administrative rank just one-half rank below Sino-Construction International. The engineering bureaus varied significantly in terms of their number of employees, assets, capital, revenues, and portfolios of domestic and overseas projects.

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<sup>224</sup> "Sino-Construction International: 10 Years of Development Overseas," exhibition in company lobby; company document.

<sup>225</sup> This organizational structure was a legacy of Sino-Construction's early history, in which the engineering bureaus carried out infrastructure projects in different parts of China to advance national industrialization. Many individuals in a given engineering bureau still hailed from the localities in which they were based.

### *Sino-Engineering and Sino-Engineering International*

Sino-Engineering was the second of the two central state-owned companies merged to create China Building Company in 2011. Sino-Engineering ranked among the top engineering design firms in China, and it held the majority of domestic market share. Sino-Engineering established Sino-Engineering International in 2007 as a flagship subsidiary responsible for expanding and managing overseas business. Sino-Engineering International's particular expertise was renewable and clean energy projects, such as solar and wind power. Sino-Engineering and Sino-Engineering International each had their own separate offices in Beijing.

### *Design Institutes*

Sino-Engineering also had eight design institutes that were responsible for project engineering design and planning. Like the engineering bureaus, the design institutes had offices located across China. In addition to executing engineering designs, feasibility studies, and economic assessments for China Building Company's projects at home and overseas, the design institutes also participated in developing new engineering technologies, setting national industry standards, and carrying out macro-level policy research.

### *Vertical Responsibility and Authority Relationships*

The chairmen of China Building Company exercise political leadership within internal organizational hierarchies characterized by vertical responsibility and authority

relationships. Sub-contracting relationships based on annual targets assigned by SASAC knit the multiple levels of the company together, from the holding company down to individual personnel. As employees worked to achieve these targets, vertical authority relationships structured their interactions and work on a day-to-day basis. These vertical authority relationships operated through a top-down system of administrative approvals and through official document flows.

Just as subcontracting defines the relationship between individual central state-owned enterprises and SASAC, it also generates relationships of responsibility among intra-firm entities.<sup>226</sup> SASAC sets annual targets for China Building Company—the most important being the total value of contracts signed during a given year—based on the previous year’s performance and other factors.<sup>227</sup> The holding company of China Building Company then broke this total target down into smaller targets and apportioned them to member companies, which in turn allocated them among their departments responsible for sales and production. Meeting—or preferably, exceeding—the SASAC targets is essential for the heads of central state-owned enterprises to be promoted. Likewise, member companies and their departments must meet these targets in order for their staff to receive annual bonuses and in order for their heads to be appraised favorably within the enterprise.

The subcontracting relationships between China Building Company and its member companies are formalized in contracts between the China Building Company

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<sup>226</sup> These subcontracting relationships are analogous to those that exist between the center and local governments in China. 周黎安 [Zhou Li-an]: 《转型中的地方政府:官员激励与治理》 [Local Government in Transition: Official Incentives and Governance] (Shanghai: Gezhi chubanshe, 2008).

<sup>227</sup> Other specific targets for central state-owned enterprise performance mandated by SASAC pertain to operational revenue, profits, economic value added (EVA), and percentage of state-owned assets preserved (国有资产保值增值率, *guoyou zichan baozhi zengzhi lv*).

leadership and the heads of its member companies and their departments. While the most important contract concerns annual performance targets, other contracts are also signed regarding issues such as Party building work, production safety, and anti-corruption efforts. Signed and stamped with the company seal, these contracts were compiled, printed and distributed internally in a booklet titled “Work Tasks and Responsibilities.” As an employee of Sino-Construction International observed: “We all have targets, going down even below the level of what you have observed with the departments signing contracts with the holding company. Within each department responsible for the markets of a particular geographic region, the targets go down to different country groups and then even goals for each person, defined as a specific dollar amount.”<sup>228</sup> Weekly updates tracking regional departments’ progress in meeting their allocated targets were circulated electronically among employees, posted in individual departments in hard copy, and displayed on electronic signboards in the corridors on each floor of the office. These updates explicitly and publicly ranked departments against one another on the basis of their progress in reaching allocated targets.

In parallel with these vertical responsibility relationships, vertical authority relationships structure employee interactions and work on a day-to-day basis. Employees addressed anyone with the position of department vice-manager or manager and above by both their name and their official title. For example, a manager surnamed “Zhang” should be addressed as “Manager Zhang” (张总, *Zhang zong*, short for 张总经理, *Zhang zongjingli*). Employees explained that in a telephone call with a

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<sup>228</sup> Sino-Construction International employee, Beijing, September 2014.

higher-ranked superior, the lower-ranked person must never hang up the call first. In meetings, one was to refrain from speaking unless a superior solicited views from attendees. “I have learned to say less unless I am invited to speak,” an employee of Sino-Construction International confided, adding: “Leaders don’t like talk and not action.”<sup>229</sup> Large, highly detailed telephone trees adorned nearly every work cubicle, giving the names and contact information for the personnel of all headquarters departments of Sino-Construction International. These telephone trees clearly detailed how individuals within each department were organized and ranked relative to one another.<sup>230</sup>

From the chairman of China Building Company down to the lowest-ranking employees, internal approvals are the everyday substance of vertical authority relationships. The company referred to this practice as “signature and reporting” (签报, *qianbao*) and considered it a critical means to “seek leaders’ guidance and report on work, update on the situation, answer queries and solve problems.”<sup>231</sup> Approvals ranged from informal oral approvals from a single individual to formal written approvals requiring the signatures of as many as six people, and they were requisite for company matters both large and small. For example, the head of Sino-Construction International signed off on everything from multi-million dollar investments to travel plans for individual senior employees. At one meeting I attended, ten minutes were spent discussing the addition of a single word to a header on the company’s online profile; it was ultimately decided that the head of Sino-Construction International

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<sup>229</sup> Sino-Construction International employee, Beijing, March 2014.

<sup>230</sup> For example, the telephone trees listed the employees for each department by the work groups to which they belonged and noted the leaders of the work groups.

<sup>231</sup> Company document, February 2015.

needed to approve the change.<sup>232</sup> Despite the inefficiencies generated by the high frequency and scope of issues requiring executive approval, company leaders were loath to relinquish this authority. As a department manager observed: “What leaders can influence most in the company is the delegation of power. ... One [of a company’s leaders] could absolutely release power of approvals and then just evaluate [outcomes] with criteria.”<sup>233</sup>

Subordinates’ desire to avoid risk further reinforced the vertical exercise of authority within China Building Company. In the absence of obtaining approval from superiors, following standard operating procedures (流程, *liucheng*) was a key method of risk avoidance. Employees shied from acting without permission or clear guidelines, as this would entail their taking responsibility and subsequently being held accountable for the outcome. It was better to do nothing than to act and make a mistake. As one employee complained: “Nobody wants to take responsibility. ... The result is that people are frozen and focus only on very precise areas of their responsibility.”<sup>234</sup> On a day-to-day basis, employees worked within vertical authority relationships. As one shared: “We don’t try to understand the whole picture. Better to think simply and focus on your own part within the larger company.”<sup>235</sup> Obtaining approval from superiors and, in its absence, adhering to standard operating procedures were key elements in the vertical authority relationships that characterized China Building Company’s operations.

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<sup>232</sup> Sino-Construction International meeting, Beijing, April 2014.

<sup>233</sup> Sino-Construction International employee, Beijing, February 2015 (English).

<sup>234</sup> Sino-Construction International employee, Beijing, February 2014 (English).

<sup>235</sup> Sino-Construction International employee, Beijing, April 2014 (English).

Official documents (公文, *gongwen*) were another routine administrative practice through which vertical authority relationships within China Building Company were constructed and maintained. Various entities within the company—from the holding company to member companies to their individual departments—would release official documents addressing a range of internal matters. Following a standard internal approvals process between the intra-firm entity issuing the official document and multiple administrative superiors, official documents were then distributed electronically through the company’s internal network. Company leaders used official documents to ensure compliance because each receiving department was required to sign them and attest that they had carried out its content. Official documents sought to guide subordinates’ behavior on a range of topics, from implementation of company work plans, to safety guidelines, to use of official company cars. Each official document was ranked on a three-level scale of importance—ordinary, urgent, and extremely urgent—with a corresponding processing time.<sup>236</sup> The company evaluated intra-firm entities on official document management and quality as part of their annual performance assessment; it threatened criticism by public circular (通报批评, *tongbao piping*) of any entities with poor performance and any individuals who held up their processing.<sup>237</sup>

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<sup>236</sup> The rules for processing times were ten days for official documents designated as “ordinary,” five days for those designated as “urgent,” and three days for those designated as “extremely urgent.” Company document, December 2014.

<sup>237</sup> Company document, December 2014.



### ***Case 1: Mr. Chen's Chairmanship***

#### *Political Leadership*

Mr. Aiwen Chen was the first chairman of China Building Company. Since Sino-Construction was the larger of the two firms merged to create China Building Company in 2011, its chairman (Mr. Chen) became the new company's chairman. Born in the early 1950s, Mr. Chen did not have an engineering background; he held a graduate degree from the Central Party School and later earned an executive MBA degree from a leading Chinese university. He build his career in one of the company's engineering bureaus over a period of decades, advancing from a technician to deputy chief, to deputy director, to assistant director and deputy chief economist, and finally to deputy director and chief economist. He impressed employees as down-to-earth and approachable but occasionally temperamental.<sup>238</sup>

Mr. Chen advocated a market-oriented, bottom-up strategy for China Building Company's development. In his first speech as chairman, he articulated an ambitious vision of "big enterprise group, big public works, big market, big brand."<sup>239</sup> To achieve this, he proposed the strategy of "prioritize the international, coordinate with the domestic." Mr. Chen's strategy gave member companies, especially engineering bureaus, a leading role in "going out" to develop overseas markets and thereby strengthening themselves through international competition. He said: "First, we need to reform the international marketing model from the original way of a single legal person signing [contracts] and centralized marketing to a new system, a new model

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<sup>238</sup> I was struck to see that Mr. Chen ate regularly in the cafeteria reserved for general employees, not in the separate cafeteria designated for company leaders.

<sup>239</sup> Speech by Mr. Chen at China Building Company's first meeting of cadres, September 2011.

that organically combines Sino-Construction International conducting centralized marketing together with member companies that meet conditions engaging in autonomous marketing. ... Relying on the platform of Sino-Construction International to develop 84 countries, is it possible to do so deeply, excellently, and widely?”<sup>240</sup> Mr. Chen warned that if China Building Company did not adopt this new approach, then “we will still have the situation of Sino-Engineering International getting projects and delegating them to the engineering bureaus for construction, and we will lose this development opportunity.”<sup>241</sup>

Markets were paramount in determining both organizational strategy and structure for Mr. Chen. He contended: “We should recognize that market demand decides strategy, strategy decides organizational structure, resource allocation, management models, operational mechanisms, and business procedures.”<sup>242</sup> Mr. Chen stated: “The main task of member companies is to respond to market demands and, expressing their function as market actors, to do everything possible to guarantee markets, guarantee contracts, guarantee development.”<sup>243</sup> He ordered “the devolution of international business management and daily operations to the front,” with headquarters to retain authority for major operational decisions and major risk control, encouraging “those [member] companies to autonomously develop international business” and serve as “model vanguard troops.”<sup>244</sup> Instead of viewing member

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<sup>240</sup> Speech by Mr. Chen at the Sino-Construction International 2013 work meeting and 4<sup>th</sup> annual meeting of employee representatives, February 2013.

<sup>241</sup> Ibid.

<sup>242</sup> Speech by Mr. Chen at the China Building Company 2012 mid-year work meeting, July 2012.

<sup>243</sup> Speech by Mr. Chen at China Building Company’s first meeting of cadres, September 2011.

<sup>244</sup> Speech by Mr. Chen at the China Building Company 2012 mid-year work meeting, July 2012.

companies as subservient entities, he emphasized their autonomy, rights, and responsibilities.<sup>245</sup>

Mr. Chen also modified China Building Company's organizational structure by changing existing authority relations and allocations of assets and personnel. The most significant change to China Building Company's organizational structure during Mr. Chen's leadership was an increase in the administrative rank of the engineering bureaus. The engineering bureaus went from being subsidiaries of Sino-Construction International to become subsidiaries of China Building Company under its direct authority—just one-half administrative rank below Sino-Construction International itself (see Figure 3.2 above). For the first time, Mr. Chen granted the engineering bureaus authority to carry out “autonomous marketing” (自主营销, *zizhu yingxiao*) for most overseas markets, with the ultimate goal of “autonomous operations” (自主经营, *zizhu jingying*). Of the 16 engineering bureaus, 14 were assigned country markets abroad; Sino-Construction International retained centralized marketing authority for only a single region. He affirmed the engineering bureaus' market autonomy by authorizing them to sign contracts in their own name for projects with a contract value of \$50 million or below. At the same time, he emphasized the “Four Unifies”: “unify brand management,” “unify market distribution and sales,” “unify regulatory compliance,” and “unify risk prevention.”<sup>246</sup> Through these organizational changes

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<sup>245</sup> As Mr. Chen asserted: “According to laws and regulations and the company charter, member companies enjoy effective corporate governance rights and full operational autonomy; they are independent actors in market competition responsible for profits and losses, and they independently assume legal responsibilities.” Speech by Mr. Chen at China Building Company's first meeting of cadres, September 2011.

<sup>246</sup> Chen's speeches and annual company work plans throughout his leadership tenure featured the “Four Unifies.”

and his bottom-up strategy, Mr. Chen aimed to transform the member companies of China Building Company from what he described as dispersed “small ships” setting sail into a massive “aircraft carrier.”<sup>247</sup>

### *Global Expansion Efforts*

Mr. Chen’s political leadership—his bottom-up strategy and changes to organizational structure to boost engineering companies’ market autonomy—yielded market-oriented global expansion efforts. Engineering bureaus led the charge overseas, with financial, administrative, and personnel support from the holding company.<sup>248</sup> For example, the First Engineering Bureau went from having one international project under construction in 2011 to having five international projects under construction in 2013.<sup>249</sup> The Eighth Engineering Bureau more than doubled its number of newly signed international contracts from nine in 2012 to 22 in 2013.<sup>250</sup> International expansion might have been an imperative for China Building Company, but the decentralized nature and particular form of its global expansion efforts were not inevitable. For example, China Building Company could have retained the original division of labor between Sino-Construction International and the engineering bureaus, in which the former led international business development and the latter carried out project construction with minimal market autonomy. Or it might have supported the

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<sup>247</sup> Mr. Chen used the “small ships” and “aircraft carrier” metaphors in an op-ed in a major Chinese state-owned newspaper in 2009.

<sup>248</sup> Some engineering bureaus had previous experience with international assistance projects (援外项目, *yuan wai xiangmu*) as early as the 1960s and began to participate in commercial projects overseas beginning in the late 1980s; however, prior to the merger they did this under the direction of Sino-Construction as its subsidiaries and therefore had limited market autonomy.

<sup>249</sup> *Sino-Engineering Company Yearbook: 2012* (Beijing, 2012); *Sino-Engineering Company Yearbook: 2014* (Beijing, 2015).

<sup>250</sup> *Ibid.*

largest and most internationally experienced engineering bureaus to specialize in overseas markets, instead of supporting all engineering bureaus to “go out”—including those with little experience in overseas markets. Within several year’s time, China Building Company’s global expansion efforts came to appear less like an aircraft carrier steaming forward than a competition among sailboats tacking their own ways toward shifting winds of market opportunity.

### *Shifts in Influence Among Intra-firm Entities*

Mr. Chen’s political leadership transformed the balance of power among intra-firm entities by boosting the influence of market-oriented actors, especially the engineering bureaus. His strategy and changes to organizational structure increased the engineering bureaus’ autonomy both in international markets and relative to Sino-Construction International. Newly empowered to “go out” and no longer subsidiaries of Sino-Construction International, the engineering bureaus increasingly felt that the holding company was now the entity to which they should turn, not only for project approvals but also for relationship and information resources. As an engineering bureau manager related: “Before Sino-Construction International had a lot of power. It was them that issued official seals and signatures, that had capital. Everything they said went. ... But now we don’t need them anymore.”<sup>251</sup> Sino-Construction International keenly felt its decreased authority over the engineering bureaus. When I requested leave to travel outside of Beijing to visit an engineering bureau, my department supervisor joked with an undertone of frustration: “Why do you want to go visit them? They are trying to

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<sup>251</sup> Engineering bureau employee, Tianjin, February 2015.

take our food away and eat it!”<sup>252</sup> Another Sino-Construction International employee expressed irritation that when some of the engineering bureaus met with current or prospective clients, they passed out introduction pamphlets about their own bureaus rather than those about China Building Company as a whole.<sup>253</sup>

However, Mr. Chen’s political leadership did not have a major impact on the influence and interactions of all intra-firm entities. Employees of Sino-Engineering and Sino-Engineering International still worked separately at different office buildings in Beijing, separate from China Building Company’s headquarters. Their cooperation with Sino-Construction International remained limited to specific projects, just as it had been before the merger and creation of China Building Company.<sup>254</sup>

#### *Intra-firm Entities’ Conceptualization of Relationship to International Markets*

During Mr. Chen’s chairmanship, intra-firm entities conceptualized their relationship to international markets using the concepts “front party” (前方, *qian fang*) and “back party” (后方, *hou fang*) (see Table 3.1 below). Their logic was simple: the “front party” included all workers based overseas, who were mostly engineering bureau employees, while the “back party” included all employees based in China, both in Beijing and in the engineering bureaus and design institutes located across the country. Employees at China Building Company’s offices in Beijing often referred to the “front party” and the “back party” in conversations with one another and in their telephone

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<sup>252</sup> Sino-Construction International employee, Beijing, January 2015.

<sup>253</sup> Sino-Construction International employee, Beijing, May 2014.

<sup>254</sup> Prior to the merger and establishment of China Building Company, Sino-Construction International contracted with the design institutes of Sino-Engineering for engineering designs for some of their bids and projects, and Sino-Engineering International contracted with the engineering bureaus for overseas project construction.

and written communications with coworkers overseas. This binary conceptualization originated organically as China Building Company expanded abroad. It reflected the emergence of a market-oriented way of thinking in which intra-firm entities reoriented their understanding of how they related to one another as the result of profound changes in their operating environments. Specifically, they were pivoting from the domestic market, in which China Building Company enjoyed direct government support through state-funded infrastructure projects, toward a new “front” in an intense battle for international market share against established foreign rivals like Bechtel and Hyundai, as well as other Chinese firms.<sup>255</sup> With regard to China Building Company’s domestic operations, intra-firm entities distinguished only between those “on-site” at a project (在现场, *zai xianchang*) and those who were not. They did not use the concepts “front party” and “back party,” because no distinct, external international markets “front” existed at that time.

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<sup>255</sup> Prior to the initiation of market-oriented reforms in 1978, the Chinese government assigned contractors construction work; there was neither a competitive market for construction projects nor a formal relationship between “contractor” and “client.” Ping Lan, “Management in the Chinese Construction Industry,” *China’s Managerial Revolution*, ed. Malcolm Warner (London: Frank Cass, 1999): 94-118.

Table 3.1: Mr. Chen’s Chairmanship: Intra-firm Entities’ Conceptualization of Relationship to International Markets

| Party          | Actors  | Functions  |
|----------------|---|--|
| <b>‘Front’</b> | <ul style="list-style-type: none"> <li>• Engineering bureaus (primary)</li> <li>• Sino-Construction International and Sino-Engineering International staff based overseas</li> </ul>                | <ul style="list-style-type: none"> <li>• Marketing</li> <li>• Project construction and supervision</li> </ul>  |
| <b>‘Back’</b>  | <ul style="list-style-type: none"> <li>• Holding company</li> <li>• Sino-Construction International and Sino-Engineering International staff based in China</li> <li>• Design institutes</li> </ul> | <ul style="list-style-type: none"> <li>• Marketing support</li> <li>• Project financing</li> <li>• Engineering and design</li> <li>• Administration (accounting, human resources)</li> </ul> |

### ***Case 2: Mr. Wu’s Chairmanship***

#### *Political Leadership*

In January 2015, China Building Company announced that Mr. Aiwen Wu would become the new chairman, because Mr. Chen had reached the mandatory retirement age of 60. Mr. Wu’s appointment was expected; he was already second in command as the Party Secretary and general manager of China Building Company. Moreover, Mr. Wu had previously served as the chairman of Sino-Engineering—the other central state-owned company merged with Sino-Construction in 2011 to create China Building Company. At the time of the 2011 merger, because Sino-Construction was the larger of the two companies, SASAC tapped its leader—Mr. Chen—to head the



newly created conglomerate. However, it was widely acknowledged, even during Mr. Chen's leadership tenure, that Mr. Wu was the "heir apparent."<sup>256</sup>

Mr. Wu differed from Mr. Chen in his educational background, professional experience, and leadership style. Born in the late 1950s, Mr. Wu held a master's degree in engineering from a leading government research institution. Before joining Sino-Engineering, he served in multiple roles conducting surveying, engineering design, and planning for a government ministry, working at both provincial and central levels. He also served as vice-president of one of the most prestigious engineering design institutes in China, and regularly published articles in leading industry magazines. Mr. Wu impressed employees as an intellectual and relatively reserved, and he was known for embellishing his speeches with literary sayings.

Mr. Wu exercised political leadership through the same methods as Mr. Chen: determining specific strategies for China Building Company's development and modifying its organizational structure. After assuming leadership, he wasted little time distinguishing himself from his predecessor with a new strategy for the company's development. Mr. Wu proposed a two-part strategy: "planning and design come first, technology leads." This strategy reflected Mr. Wu's ambition to sequence, standardize, and control the company's development, while at the same time increasing its prioritization of engineering and technological expertise. To Mr. Chen's "4 Unifies," Mr. Wu quickly added a fifth—"unify strategic design"—and put it in first place.<sup>257</sup> Mr. Wu envisioned that a single chain of command—originating from company

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<sup>256</sup> Former Sino-Construction International employee, Beijing, May 2016.

<sup>257</sup> Mr. Chen's "Four Unifies" were: "unify brand management," "unify market distribution and sales," "unify regulatory compliance," and "unify risk prevention." Company document.

headquarters—would direct international business, instead of “many guns firing at a single bird.”<sup>258</sup> Mr. Wu’s new development strategy aimed to rectify what an internal summary of the company’s work in 2015 listed as its problems: “many actors engaged in market operations, scattered resources for international business, and internal duplication and competition.”<sup>259</sup>

Mr. Wu also carried out major changes to organizational structure. In 2016, he presided over the largest internal restructuring of China Building Company since its establishment: the creation of China Building Company International (CBC International).<sup>260</sup> Its stated aim was twofold: 1.) to increase the company’s competitiveness by deepening the vertical industry integration that had originally motivated China Building Company’s own establishment; and 2.) to consolidate the enterprise group’s resources for international business. Specifically, CBC International amalgamated three entities: Sino-Construction International, Sino-Engineering International, and the Overseas Business Department (see Figure 3.3).<sup>261</sup> CBC International became the sole entity authorized to control all of China Building

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<sup>258</sup> China Building Company 2016 Work Plan.

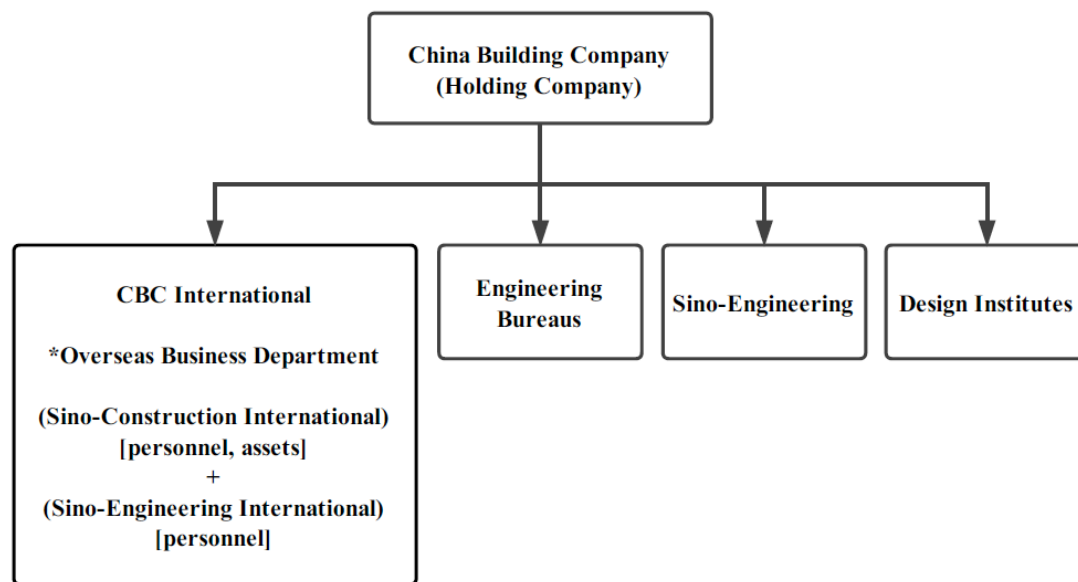
<sup>259</sup> Company document, March 2016.

<sup>260</sup> While discussions about the creation of CBC International had begun several years prior, Mr. Wu determined many of its central aspects amid intense internal debate, including its formal organizational structure and the appointment of key personnel. For example, an employee noted that the numbers and authority of Sino-Engineering employees in CBC International were both significantly greater than in early discussions during Mr. Chen’s leadership term. Former Sino-Construction International employee, Beijing, May 2016.

<sup>261</sup> The Overseas Business Department was a department with highest authority for the coordination of company affairs related to international business, such as: implementing operational planning and targets; guiding member companies’ international projects; facilitating project bidding and contract negotiations and signing; and formulating the company’s management rules for international work. After the establishment of China Building Company in 2011 and prior to the creation of CBC International in 2016, the Overseas Business Department was part of the holding company. *Sino-Construction International: Chronicle of Organizational Structure (1950-2011)* (Beijing, 2013).

Company's overseas business and to manage all of its offices abroad.<sup>262</sup> In short, the creation of CBC International represented both the consolidation of physical assets as well as the “soft centralization” of organizational authority for international business.<sup>263</sup>

Figure 3.3: Organizational Structure of China Building Company, During Mr. Wu's Chairmanship



(\*The design institutes were placed directly under the holding company's administration in 2014)

### *Global Expansion Efforts*

Mr. Wu's political leadership significantly decreased the level of marketization of global expansion efforts within just one year. Previously, Mr. Chen had empowered engineering bureaus to “go all out,” literally and figuratively, to develop various

<sup>262</sup> Company document, March 2016.

<sup>263</sup> Andrew C. Mertha, “China's ‘Soft’ Centralization: Shifting *Tiao/Kuai* Authority Relations,” *The China Quarterly* 184 (2005): 791-810.

country markets overseas. In contrast, global expansion efforts under Mr. Wu's leadership became increasingly administrative, as the holding company directed them from the top down through CBC International. When I asked a CBC International employee in May 2016 which overseas markets a particular engineering bureau was responsible for, he reprimanded: "We don't talk about the country markets of engineering bureaus anymore."<sup>264</sup> As an engineering bureau manager described the change in China Building Company's global expansion efforts: "Under Mr. Chen, the engineering bureaus played a guiding role, [it was their work that] propelled design. Under Mr. Wu, now design plays a guiding role and design propels the engineering bureaus."<sup>265</sup> As an example of this, employees described a proposal to dispatch engineering teams from Sino-Engineering to tour foreign countries and recommend possible infrastructure projects to their governments, instead of foreign governments putting forward particular projects for potential cooperation based on their own national development plans.<sup>266</sup> An internal summary of the company's work in 2015 touted its drafting of such a development plan for a province in Pakistan and noted that similar efforts were ongoing for multiple other countries.<sup>267</sup>

### *Shifts in Influence Among Intra-firm Entities*

Mr. Wu's political leadership also reshaped the balance of power among intra-firm entities. Administrative actors within the firm—the holding company, Sino-

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<sup>264</sup> CBC International employee (former Sino-Construction International and engineering bureau employee), Beijing, May 2016.

<sup>265</sup> Engineering bureau employee, Tianjin, June 2016.

<sup>266</sup> CBC International employee (former Sino-Construction International employee), Beijing, May 2016.

<sup>267</sup> Company document, March 2016.

Engineering, and design institutes—gained influence, while market-oriented actors—the former Sino-Construction International and especially the engineering bureaus—lost influence. Under Mr. Wu, the holding company acted quickly to restrain the engineering bureaus’ market autonomy. As an engineering bureau manager bemoaned: “In the beginning we found our own projects and made our own contacts, we could develop spontaneously. ... Our room for development now is being greatly limited. For everything we must listen to the holding company. We are being controlled to death.”<sup>268</sup> Mr. Wu’s strategy of “planning and design come first, technology leads” inverted the prioritization that Mr. Chen previously granted to the engineering bureaus and instead implicitly accorded it to Sino-Engineering and the design institutes. While the competitive relationship among engineering bureaus remained, it was now subordinated to their struggles for autonomy relative to the holding company.

Sino-Construction International too lost out, because its combination with Sino-Engineering International in the newly created CBC International weakened its autonomous influence. Mr. Wu tapped Sino-Engineering International’s offices as the temporary headquarters of CBC International and transferred most of Sino-Construction International’s staff there. Amidst tensions during what employees of the former Sino-Construction International and Sino-Engineering International both described as a “period of mutual adjustment” (磨合期, *mohe qi*), they began to work together in the same place on the same projects for the first time. But instead of the newly-formed CBC International becoming a larger and more influential counterweight to the holding company, Mr. Wu made clear it would remain

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<sup>268</sup> Engineering bureau employee, Tianjin, June 2016.

subordinate to the holding company's direction. As a former Sino-Construction International employee complained: "Before we had the authority to make project-level decisions, but now we are being treated basically as a marketing department with some of the previous authority we had for project-level decisions now being moved to the holding company level."<sup>269</sup>

In contrast, Sino-Engineering and the design institutes felt their position was ascendant. A Sino-Engineering employee emphasized that "design takes the lead" (设计是龙头, *sheji shi longtou*), contending that the role of design was more important than project construction and moreover that each should take its own place: "Design is design, and construction is construction."<sup>270</sup> This separation of roles and the implicit hierarchy accorded to them clearly put Sino-Engineering and the design institutes in the most advantageous position under Mr. Wu's leadership. Another employee described the new hierarchy among China Building Company's various intra-firm entities even more directly: "The position of the design institutes is the highest—they put forward the thinking (提思想, *ti sixiang*). Next is CBC International, they are responsible for implementation. And next is the engineering bureaus, they do the actual work."<sup>271</sup>

#### *Intra-firm Entities' Conceptualization of Relationship to International Markets*

Mr. Wu's political leadership also partially changed how intra-firm entities conceptualized their relationship to international markets (see Table 3.2). While those

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<sup>269</sup> CBC International employee (former Sino-Construction International employee), Beijing, May 2016.

<sup>270</sup> Sino-Engineering employee, Beijing, June 2016.

<sup>271</sup> CBC International employee (former Sino-Engineering employee), Beijing, June 2016.

physically overseas remained the “front party,” back in China employees of the newly-created CBC International now officially described themselves as a “middle party” (中方, *zhong fang*) or a “middle-back platform” (中后台, *zhong hou tai*). This “middle party” was responsible for a range of market-serving functions distinct from the purely administrative duties of the “back party,” such as technical design and assisting clients with project financing from Chinese financial institutions. As a CBC International employee described: “The ‘front party’ is the core of overseas expansion, the ‘middle party’ is the tool to advance market opening, and the back party provides its necessary logistics guarantee.”<sup>272</sup>

From the outside, it might appear that the emergence of the concept of a “middle party” indicated greater decentralization, because a portion of the “back party” had moved toward the market. But in fact this shift too showed the recentralization of authority wrought by Mr. Wu’s strategy of “planning and design come first, technology leads” and internal organizational changes caused by CBC International’s establishment.<sup>273</sup> Administrative superiors imposed the concept of “middle party”; employees did not come up with it themselves. This was evidenced by the suddenness with which the term appeared and the confusion among employees about the entities it included and their specific functions.<sup>274</sup> Some persisted in using

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<sup>272</sup> CBC International employee (former Sino-Construction International employee), Beijing, May 2016.

<sup>273</sup> The creation of CBC International also involved the establishment of four new technology departments responsible for developing and applying technological expertise relevant to the company’s various business lines.

<sup>274</sup> I listed “front party,” “middle party,” and “back party” and asked respondents to first fill in the intra-firm entities they comprised, their specific functions, and then explain their relationship in an anonymous questionnaire that I distributed to a convenience sample of CBC International employees three months after its creation. Employee-provided definitions of the functions of the “middle party” ranged from project planning to project management to technical support to “doing what is necessary” to coordinate market development and support the “front party.” More tellingly, several respondents

the old binary way of thinking, simply combining the “middle party” and “back party” together. For example, one employee explained metaphorically: “the front party fights battles and the middle and back parties support it by foraging for food and grass” (前方打仗，中后方粮草支持, *qian fang dazhang, zhong hou fang liangcao zhichi*).<sup>275</sup>

Table 3.2: Mr. Wu’s Chairmanship: Intra-firm Entities’ Conceptualization of Relationship to International Markets

| Party           | Actors   | Functions  |
|-----------------|--|--|
| <b>‘Front’</b>  | <ul style="list-style-type: none"> <li>• Engineering bureaus</li> <li>• CBC International staff based overseas</li> </ul>  | <ul style="list-style-type: none"> <li>• Project construction and supervision</li> <li>• Marketing support</li> </ul>        |
| <b>‘Middle’</b> | <ul style="list-style-type: none"> <li>• CBC International staff based in China (*including former Sino-Construction International and Sino-Engineering International staff)</li> <li>• Design institutes</li> </ul> | <ul style="list-style-type: none"> <li>• Marketing</li> <li>• Project financing</li> <li>• Engineering and design</li> </ul> |
| <b>‘Back’</b>   | <ul style="list-style-type: none"> <li>• Holding company</li> </ul>  | <ul style="list-style-type: none"> <li>• Administration (accounting, human resources)</li> </ul>                             |

### *Putting Political Leadership into Action: Five Tactics*

Both chairmen’s political leadership—their choices about organizational strategy and structure—created different sets of winners and losers within China Building Company. As Mr. Chen himself observed: “Reform and innovation will inevitably break up the existing configuration of interests. ... For a company this means that a

defined “front party” and “back party” but left “middle party” blank. Author’s “Research Questionnaire,” June 2016.

<sup>275</sup> CBC International employee, written response to author’s “Research Questionnaire,” June 2016.



top-down force at the company level is needed to break resistance and advance reform and innovation, to adjust production relations, and to stimulate new vitality.”<sup>276</sup> How specifically do heads of public sector organizations in China overcome potential internal resistance in order to carry out their preferred agendas and generate organizational change? China Building Company’s experience of economic reform suggests they use multiple tactics, including: personnel ploys, emphasis on material and status gains, invocation of external threats, underscoring of administrative superiors’ directives, and appeals to personal duty and morality. Different organization heads may employ several of the same tactics, even if their political leadership—the choices they make about organizational strategy and structure—varies widely.

Personnel ploys occur when an organizational leader appoints his allies to key leadership posts.<sup>277</sup> These formal micro-level moves reshape informal networks of patronage relationships, in which allies exchange their allegiance to the organizational leader in return for tangible and/or intangible individual benefits.<sup>278</sup> Personnel ploys can bolster an organizational leader’s influence because they break up existing

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<sup>276</sup> Speech by Mr. Chen at Sino-Construction International’s 2011 mid-year work meeting, August 2011.

<sup>277</sup> Such alliances may be based on multiple factors, such as shared work or educational experiences, regional identities, professional identities, gender, and/or family ties. For example, imagine a case in which the head of a central state-owned enterprise and his ally both originated from the same province in China and worked there together as engineers in the same engineering bureau.

<sup>278</sup> On other forms of clientelism, such as prebends and tribute, see Nicolas van de Walle, “Meet the New Boss, Same As the Old Boss? The Evolution of Political Clientelism in Africa,” *Patrons, Clients and Policies: Patterns of Democratic Accountability and Political Competition*, eds. Herbert Kitschelt and Steven I. Wilkinson (Cambridge: Cambridge University Press, 2007): 50-67. On patronage relationships in China, see Farh et al 1998, Hillman 2014, Paik and Baum 2014, and Walder 1988. Jiing-Lih Farh, Anne S. Tsui, Katherine Xin, and Bor-Shiuan Cheng, “The Influence of Relational Demography and *Guanxi*: The Chinese Case,” *Organization Science* 9, no. 4 (1998): 471-488; Ben Hillman, *Patronage and Power: Local State Networks and Party-State Resilience in Rural China* (Palo Alto, CA: Stanford University Press, 2014); Wooyeal Paik and Richard Baum, “Clientelism with Chinese Characteristics: Local Patronage Networks in Post-Reform China,” *Political Science Quarterly* 129, no. 4 (2014): 675-702; Andrew G. Walder, *Communist Neo-traditionalism: Work and Authority in Chinese Industry* (Berkeley, CA: University of California Press, 1988).

patterns of influence while simultaneously building a network of allies through which he can affect decision-making, shape resource allocation, coordinate intra-organizational units' behavior, and obtain information.<sup>279</sup> In China Building Company, personnel ploys entailed the chairman posting his allies—either close personal contacts or those who belonged to the same company he led before the merger—to top positions in key departments and member companies.<sup>280</sup> Take for example Mr. Wu's moves after becoming chairman. He appointed a former executive of Sino-Engineering International to head the regional department of the newly created CBC International that had the largest revenues—even though that individual had far less experience in that region than his peers at Sino-Engineering International. In CBC International's reconstituted Investment Department, he created a new requirement that 50% of its employees come from Sino-Engineering, even though Sino-Engineering had accounted for less than 40% of China Building Company's total assets, revenues, profits, and personnel at the time of the 2011 merger.<sup>281</sup>

However, organizational leaders' ability to carry out personnel ploys is not without limits. Internal backlash may result if an organizational leader's appointments of allies are perceived as violating norms for professional advancement or if the individuals he appoints are viewed as unqualified for their posts. Organizational

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<sup>279</sup> On how the development of patronage networks impacts the exercise of power and its institutionalization within the state, see Catherine Boone, *Merchant Capital and the Roots of State Power in Senegal: 1930-1985* (Cambridge: Cambridge University Press, 2006).

<sup>280</sup> For Mr. Chen, this meant employees of Sino-Construction. For Mr. Wu, this meant employees of Sino-Engineering.

<sup>281</sup> Moreover, Sino-Engineering accounted for a much smaller, albeit quickly increasing, portion of the company's overall international business. In 2015, Sino-Engineering International had 12 new contracts for overseas projects with a total contract value of approximately \$5 billion, far less than Sino-Construction International's 115 new contracts for overseas projects with a total contract value of approximately \$11 billion. Company document.

leaders are also constrained in their ability to displace the employees appointed by their predecessors. In state-owned enterprises and other public sector organizations in China, it is extremely difficult to demote or to fire employees, especially those in senior positions.<sup>282</sup> This explains why in CBC International, the number of vice presidents (副总经理, *fu zongjingli*) reached an astounding 27 by the spring of 2016.<sup>283</sup> Finally, central state-owned enterprises like China Construction Company that have experienced mergers are subject to heightened levels of oversight by SASAC during and immediately following the merger. Mediation by SASAC or even disciplinary consequences are possible if personnel ploys are excessive or engender internal discord. These factors constrained the ability of central state-owned enterprise heads like Mr. Chen and Mr. Wu to appoint allies to key leadership posts within the firm.

Organization heads also seek to advance their leadership agendas by emphasizing their organizations' material and status gains, both actual and potential. This works to boost internal support because organizational success benefits individuals' material self-interest as well as their sense of self-worth. Such appeals also legitimate an organization head's political leadership by highlighting the progress already achieved during his tenure and by suggesting that subordinates' short-term allegiance and effort will earn future rewards. Both chairmen of China Building Company vowed that their development strategies and changes to organizational structure would bring future company and employee prosperity. For example, Mr.

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<sup>282</sup> Instead of firing employees, state-owned companies will typically transfer them, wait until they retire, or attempt to get them to quit on their own by limiting their existing authority and/or opportunities for future promotion.

<sup>283</sup> CBC International employee, Beijing, March 2016.

Chen promised that his new strategy for the company's development "would produce a surge effect [井喷式的效应, *jingpen shi de xiaoying*], by adjusting production relations it will release productive forces."<sup>284</sup>

Organization heads may also emphasize gains in organizational status to justify their particular choices about organizational strategy and structure. Official recognition by administrative superiors for achievements in a particular area is one important type of gain in organizational status. For example, Mr. Chen highlighted that SASAC awarded China Building Company the "Outstanding Enterprise Performance Prize" (业绩优秀企业奖, *yeji youxiu qiye jiang*) and an annual "A grade" evaluation under his leadership.<sup>285</sup> Gains in organizational status also include increases in domestic or international rankings. For example, Mr. Wu emphasized China Building Company's rapid advancement in the Fortune Global 500 rankings during his tenure as chairman. The company jumped 60 ranks in 2015, the first year of Mr. Wu's chairmanship, and again rose more than 50 ranks in 2016. Mr. Wu cited these organizational status gains in the first sentence of a speech recapping the company's work in 2016 as evidence of its "remarkable production and operation results" and "steadily rising global influence" under his leadership.<sup>286</sup>

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<sup>284</sup> Speech by Mr. Chen at the Sino-Construction International 2013 work meeting and annual meeting of employee representatives, February 2013.

<sup>285</sup> Speech by Mr. Chen at China Building Company's 2014 work meeting, February 2014. Other special prizes that SASAC awards to central state-owned enterprises are the "Technology and Innovation Enterprise Prize" (科技创新企业奖, *keji chuangxin qiye jiang*), the "Managerial Advances Enterprise Prize" (管理进步企业奖, *guanli jinbu qiye jiang*), and the "Outstanding Energy Saving and Emissions Reductions Enterprise Prize" (节能减排优秀企业奖, *jienerg jianpai youxiu qiye jiang*). SASAC: 《中央企业负责人经营业绩考核暂行办法》 [Interim Measures for Operational Performance Assessment of Central State-owned Enterprise Principals], December 28, 2009.

<sup>286</sup> Speech by Mr. Wu reviewing the company's important work in 2016, January 2017.

However, material or status gains that directly impact actors within an organization may have greater influence on their behavior than material or status gains for the organization as a whole. Variation in employees' degree of personal identification with the organization also mediates the extent to which organizational achievements affect their individual behavior. During the Maoist era, cellular work units (单位, *danwei*) functioned as the basic building blocks of economic production, political mobilization, and social life; they provided workers with lifetime employment, social solidarity, and a stable, recognized status.<sup>287</sup> In contrast, employees of China Building Company, especially junior personnel, now hold a far more conditional and transactional view of their relationship with their place of employment. As one employee explained: "Now Sino-Construction International is not a work unit [单位, *danwei*]. It is a company [公司, *gongsi*] only. I contribute my work and time and I get a salary—this is the deal."<sup>288</sup> Immediate, individual material benefits—salaries, bonuses, and fringe benefits—were of greater concern to many employees than overall gains in the company's performance or organizational status.<sup>289</sup> When I asked a Sino-Construction International Employee privately what motivated his efforts to achieve the company's ambitious annual targets, he answered:

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<sup>287</sup> Work units during the Mao era provided workers with numerous welfare benefits in addition to lifetime employment, including: food, housing, healthcare, childcare, education, and pensions. Xiaobo Lu and Elizabeth J. Perry, eds., *Danwei: The Changing Chinese Workplace in Historical and Comparative Perspective* (Armonk, NY: M.E. Sharpe, 1997).

<sup>288</sup> Sino-Construction International employee, Beijing, February 2015.

<sup>289</sup> Sino-Construction International employees continued to receive many fringe benefits in addition to their salaries. They included: company-issued work uniforms, shoes, and ties for men; dry cleaning credits; cell phone credits; bookstore gift cards; gift cards for the movies; union-issued credits to purchase vegetables and a gift box of meats for Chinese New Year. The company's cafeteria also provided three subsidized meals a day, ranging in cost from approximately \$1-3.50.

“Both my individual interests and our department’s pride. But mostly my individual interests.”<sup>290</sup>

Organization heads may also invoke external threats to mobilize internal support. Painting a picture of external threats benefits organizational leaders because it promotes internal unity and raises the costs for any actors who might seek to oppose or delay carrying out their leadership agendas.<sup>291</sup> These external threats may be political, social, or economic in nature, and they may be either domestic or international. For example, the chairmen of China Building Company frequently invoked rising competition, declining demand, and economic slowdown in overseas and domestic markets as a serious threat that demanded concerted action by the company and its employees to address. Some employees appeared to agree that such external threats made the implementation of enterprise heads’ leadership agendas imperative. As an employee described the logic behind the creation of CBC International several weeks after its establishment under Mr. Wu’s leadership: “If our company does not undertake these changes and be better positioned in the overseas markets, then other [Chinese] companies will do so and our company will lose this historical opportunity.”<sup>292</sup>

However, organizational leaders’ invocation of external threats may have varying impact on actors within the organization, depending on their perceptions of particular threats’ relevance and immediacy. For example, a central state-owned

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<sup>290</sup> Sino-Construction International employee, Beijing, September 2014.

<sup>291</sup> This is similar to national leaders’ strategic use of perceived international threats to mobilize domestic resources and support in order to advance particular political or economic agendas. Thomas J. Christensen, *Useful Adversaries: Grand Strategy, Domestic Mobilization, and Sino-American Conflict, 1947-1958* (Princeton, NJ: Princeton University Press, 1996); Tianbiao Zhu, “Consistent Threat, Political-Economic Institutions, and Northeast Asian Developmentalism,” (Ph.D. dissertation, Cornell University, 2000).

<sup>292</sup> CBC International employee (former holding company employee), Beijing, April 2016.

enterprise leader's emphasis on increasing international market competition may be less effective in galvanizing administrative actors within the firm compared to those carrying out market-oriented functions. Invocation of external threats may also have less impact on junior employees compared to those in mid-career and senior posts, because any failure on their part to respond successfully to external threats is ultimately their superiors' responsibility. In order for the invocation of external threats to be effective as a tactic, organizational leaders must therefore tailor the threats they invoke so that subordinates perceive them as both relevant and immediate.

Organization heads also underscore administrative superiors' directives in order to advance their own leadership agendas. This approach is effective because administrative superiors' legal authority exceeds that of any potentially opposing entities within an organization, thereby increasing the costs of opposition. Moreover, since subordinates often lack information about organization heads' communications with administrative superiors, this information asymmetry creates limited space for organization heads to selectively frame administrative superiors' directives, implementation approaches, and their consequences.<sup>293</sup>

Organization heads use administrative superiors' directives in two main ways. First, they may invoke administrative superiors' mandates in broad terms to bolster their own authority and quell potential resistance. For example, Mr. Chen emphasized that the 2011 merger was a decision of the State Council, and he urged managers to "guarantee completion of the task assigned to the organization and resolutely

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<sup>293</sup> Mitchell P. Smith, "The Commission Made Me Do It: The European Commission as a Strategic Asset in Domestic Politics," *At the Heart of the Union*, ed., Neill Nugent (London: Palgrave Macmillan UK, 1997): 167-186.

implement the overall requirements of SASAC's Party Committee for participant companies during the reorganization period: 'no chaos in thinking, no disruption in production, no dispersal of the team, no loss of state assets, and protection of corporate and social stability.'"<sup>294</sup> Second, organization heads may argue that their strategy or organizational changes will advance administrative superiors' mandates or even national policies and are therefore both justified and advisable. For example, Mr. Wu linked his strategy of "planning and design comes first, technology leads" and the associated practice of directly drafting development plans for potential clients in other localities with the Xi Jinping administration's "One Belt, One Road" and other central-level initiatives. Under Mr. Wu's leadership, the 2016 Work Plan charged the company with "on the basis of deeply researching and closely following 'One Belt One Road,' international industrial capacity cooperation [国际产能合作, *guoji channeng hezuo*], and other national strategies ... continuing to actively participate in other countries' development planning and research."<sup>295</sup> Existing concepts of "state framing" or "policy entrepreneurship" do not capture this type of discursive practice, because it is neither mere repetition of the official line nor an attempt to change the substance of existing policies.<sup>296</sup> Instead, it shows how officials in China can be

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<sup>294</sup> Speech by Mr. Chen at Sino-Construction International's 2011 meeting on operations and management work, April 2011.

<sup>295</sup> Company document, March 2016.

<sup>296</sup> On the concepts of "state framing" and "policy entrepreneurship," see Chapter 1, "China's Hydraulic Society?" in Andrew C. Mertha, *China's Water Warriors: Citizen Action and Policy Change* (Ithaca, NY: Cornell University Press, 2008); Andrew C. Mertha, "'Fragmented Authoritarianism 2.0': Political Pluralization in the Chinese Policy Process," *The China Quarterly* 200 (2009): 995-1012.



simultaneously subject to state authority while also strategically appropriating it to minimize opposition and mobilize support within their own organizational domains.<sup>297</sup>

However, while emphasis on administrative superiors' directives might help to secure overall compliance from subordinates, it offers less leverage in addressing the myriad practical challenges of carrying out specific strategies or changes to organizational structure. For example, while China Building Company employees recognized that SASAC mandated the 2011 merger, this did not minimize the impact that they perceived it had on their daily lives and professional futures. One employee expressed frustration at having had to work in four different departments in the span of two years and experiencing stalled professional advancement post-merger. "In theory we are supposed to move up one level every year," she explained, "but I have been at the company for five years and my level hasn't changed."<sup>298</sup> In addition, some entities or individuals within an organization may delay or even resist its leader's political leadership agenda—even if he invokes administrative superiors' directives—by arguing that the timing or conditions are not yet right to carry it out.

Finally, organizational leaders may appeal to personal duty and morality in order to bolster support from subordinates.<sup>299</sup> Such appeals enhance subordinates'

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<sup>297</sup> Weldes 1996 highlights the crucial role of elite manipulation by showing how elite-generated associative chains combine to produce contextually specific and contingent representations of the world. Jutta Weldes, "Constructing National Interests," *European Journal of International Relations* 2, no. 3 (1996): 275-318.

<sup>298</sup> Sino-Construction International employee, Beijing, November 2017. There were more than 50 different administrative levels within the company. Each level had a fixed based salary, starting at about 3,500 RMB (approximately \$600) per month, and advancement was linked with both performance and seniority.

<sup>299</sup> In contrast to Weber's claim that the rationalization and routinization of behavior in organizations constrains and ultimately negates such "meaning making" by charismatic leaders, others argue that leaders' importance as a source of organizational values in fact facilitates coordination and efficiency in modern organizations. Joel M. Podolny, Rakesh Khurana, and Marya Hill-Popper, "Revisiting the Meaning of Leadership," *Research in Organizational Behavior* 26 (2004): 1-36; Max Weber,

sense of self-worth and personal commitment by connecting their self-concepts and individual behavior with the realization of important shared values.<sup>300</sup> In China Building Company, organizational leaders' appeals to personal duty and morality included but also went beyond the requisite Party slogans of the time concerning individual integrity. For example, Mr. Chen emphasized employees' sense of duty and responsibility and admonished them to put the company's interests first despite organizational change. He told employees: "As the saying goes, people have self-awareness, and with self-awareness it is possible to be rational and equitable when judging gains and losses, to avoid being impetuous and irrationally feel underappreciated, and to rationally and pragmatically face change. I believe that most comrades have this type of basic quality—and also should have this type of quality."<sup>301</sup> In a similar vein, Mr. Wu called upon employees to cultivate a mindset of personal striving, an "attitude of always being on the road" (永远在路上的心态, *yongyuan zai lushang de xintai*) and to create an environment of positive public discourse for the company's reform and development.<sup>302</sup>

Yet the changing relationship between public sector organizations in China and their employees, particularly junior employees, means that personal considerations and material interest may exert greatest influence on employees' thinking and behavior—even if individuals remain reluctant to acknowledge this openly. Balancing company

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"Bureaucracy," *From Max Weber: Essays in Sociology*, eds. and trans. H. H. Gerth and C. Wright Mills (New York: Routledge, 2009 [1946]): 232-235.

<sup>300</sup> Boas Shamir, Robert J. House, and Michael B. Arthur, "The Motivational Effects of Charismatic Leadership: A Self-concept Based Theory," *Organization Science* 4, no. 4 (1993): 577-594.

<sup>301</sup> Speech by Mr. Chen at Sino-Construction International meeting for all headquarters employees, December 2011.

<sup>302</sup> Speech by Mr. Wu at China Building Company's 2017 work meeting, January 2017.

and personal interests can create particularly acute dilemmas for junior employees. For example, not all personnel are willing to spend years or even decades working overseas in often difficult locations.<sup>303</sup> One employee resigned within weeks of the company assigning him to a project in central Africa, because he was not willing to spend the next several years apart from his spouse and soon-to-be-born child.<sup>304</sup> It is becoming increasingly common for officials and employees of state-owned enterprises who work “within the system” (体制内, *tizhi nei*), to quit their jobs and cross over into private sector employment with domestic and even international companies.<sup>305</sup>

### *Alternative Explanations*

Beyond political leadership, several alternative explanations can be advanced to account for the variation over time in China Building Company’s economic reform. From a strategic design perspective, one might question whether the changes that occurred between 2011 and 2016 reflected intervention by external actors, namely administrative superiors, rather than the political leadership of Mr. Chen and Mr. Wu. Such an argument would suggest that Mr. Chen and Mr. Wu were proxies or agents of outside principals, who either dispatched them to lead the company in order to realize their interests and agendas, or to deliberately change course from Mr. Chen’s initial leadership.

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<sup>303</sup> Some of China Building Company’s project sites are so remote that they can only be reached by helicopter or plane, or so dangerous that they are fenced in and protected by local military. One senior manager described years spent working on such a project in Pakistan at the beginning of his career. Sino-Construction International employee, Beijing, February 2015.

<sup>304</sup> Sino-Construction International employee, Beijing, December 2014.

<sup>305</sup> This “system” also comprises other public sector organizations beyond state-owned enterprises, such as government departments, Party organs, research institutes, and universities.

However, the circumstances of both Mr. Chen and Mr. Wu's appointments suggest that this was not the case. Prior to the merger and creation of China Building Company in 2011, Mr. Chen had already served as the head of Sino-Construction since 2006. He became the chairman of the newly formed conglomerate because he was already the head of Sino-Construction and it was the larger of the two firms in terms of its assets, revenues, profits, and personnel. Mr. Wu later took over as chairman in 2015 because Mr. Chen had reached the mandatory retirement age of 60, and because he had already been serving as the second in command at China Building Company since its founding.<sup>306</sup> The appointments of both Mr. Chen and Mr. Wu reflected existing bureaucratic rules, not external intervention. Moreover, there is no evidence available to suggest that either of the two chairmen acted as the proxies of external actors during their tenures. Both men rose to positions of leadership after spending their entire careers working in the construction industry; unlike some other heads of central state-owned enterprises, they were not appointed from outside positions in central or local government.<sup>307</sup>

One might also suggest that another type of top-down strategic design shaped China Building Company's economic reform: major changes in policy by its administrative superiors (SASAC and the State Council). For example, perhaps SASAC issued a directive ordering central state-owned enterprises to recentralize holding companies' authority over global expansion efforts, or the State Council

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<sup>306</sup> The mandatory retirement age is 60 for Chinese officials holding positions of vice-ministerial and department-level rank is 60. The position of chairman of China Building Company is of department-level rank. Barry Naughton, "Leadership Transition and the 'Top-Level Design' of Economic Reform," Hoover Institution, China Leadership Monitor, no. 37, Spring 2012.

<sup>307</sup> Wendy Leutert, "The Political Mobility of China's Central State-owned Enterprise Leaders," *The China Quarterly*, forthcoming.

required every central state-owned enterprise to set up new departments to advance the “One Belt, One Road” initiative, like the “Transportation Department” that Mr. Wu established after becoming chairman.

However, policies since 2011 have largely affirmed central state-owned enterprises’ operational autonomy relative to their administrative superiors and even devolved it further, with several exceptions.<sup>308</sup> For example, SASAC launched pilots for state capital management in 2014, which involves granting central state-owned enterprises increased autonomy for capital management decision-making within particular state-owned business groups.<sup>309</sup> In 2017, the State Council issued new guidelines to shift SASAC’s overall function away from state-owned asset management toward state-owned capital management and supervision. These guidelines not only eliminated and devolved a number of SASAC’s administrative

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<sup>308</sup> These exceptions include: the anti-corruption campaign initiated after Xi Jinping came to power in 2012, because it has involved the Central Commission for Discipline Inspection dispatching investigators to central state-owned enterprises to carry out on-site investigations; strengthened requirements for oversight of state-owned assets in China and overseas introduced in 2016 and 2017, which mandate greater information reporting and in a small number of cases has also involved SASAC sending investigators to conduct on-site inspections; mandatory reductions to state-owned enterprise executive salaries introduced in 2015; and ongoing efforts to get central state-owned enterprises to reduce their commercial activities outside of their core business areas (especially in real estate). However, no direct link is apparent between these policies and the changes observed at China Building Company; moreover, some of these policies were initiated after these changes had already occurred. Politburo of the CCP Central Committee: 《中央管理企业负责人薪酬制度改革方案》 [Compensation Reform Plan for Heads of Enterprises Managed by the Center], January 1, 2015; State-owned Assets Supervision and Administration Commission: 《中央企业投资监督管理办法》 [Measures for the Supervision and Administration of Investment of Central State-owned Enterprises] and 《中央企业境外投资监督管理办法》 [Measures for the Supervision and Administration of Overseas Investment of Central State-owned Enterprises], January 18, 2017.

<sup>309</sup> State capital management reform also comprises a second experimental scheme in which state-owned enterprises with broad cross-industry holdings function like asset management companies, managing state-owned assets on the government’s behalf. This second type of state capital management reform commenced in 2016 when SASAC and the National Development and Reform Commission tapped China Reform Holdings Corporation and Chengtong Holdings Group Limited as pilot enterprises. The two subsequently launched funds to manage state capital and to facilitate state-owned enterprises’ restructuring, respectively. 《国资委启动四项改革试点》 [SASAC Starts Four Reform Pilots], *Xinhua News*, July 14, 2014.

functions, they affirmed specific areas in which central state-owned enterprises possess administrative rights—including the right of their heads to determine the strategies for their companies’ development.<sup>310</sup> In 2017, SASAC also announced that central state-owned enterprises will be categorized into three groups—entity industrial groups, investment companies, and operating companies—suggesting that they may enjoy greater autonomy for capital management in the future.<sup>311</sup>

An organic transformation perspective on economic reform in China points to changes in market competition as another possible explanation. Major shifts in the markets in which China Building Company operates might have triggered corresponding adaptation in organizational structures and strategies. However, there were no significant changes in the domestic construction market after China Building Company’s establishment in 2011. The number of central state-owned enterprises in the industry did not change.<sup>312</sup> Nor did the overall level of competition in the construction industry: the percentage of state-owned enterprises in the sector between 2012 and 2016 remained relatively stable, ranging between 18% and 33% during this period.<sup>313</sup> The overseas construction market did not exhibit any major fluctuations either. Between 2012 and 2015, the top 250 international contractors ranked by Engineering News-Record reported total contracting revenue from projects outside

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<sup>310</sup> State Council: 《国务院国资委以管资本为主推进职能转变方案》 [Plan for State Council State-owned Assets Supervision and Administration Commission Advancing Functional Transformation By Taking Capital Management as the Core], April 27, 2017.

<sup>311</sup> “China State-owned Enterprises to be Divided Into Three Categories,” *China Daily*, June 5, 2017.

<sup>312</sup> State-owned Assets Supervision and Administration Commission: 《中国国有资产监督管理年鉴》 [State-owned Assets Supervision and Management Yearbook] (Beijing: Zhongguo jingji chubanshe, 2012, 2013, 2014).

<sup>313</sup> I calculate levels of market competition based on the proportion of publicly listed companies on both the Shenzhen and Shanghai stock markets in a given industry for which the ultimate parent company is a state-owned enterprise, using data from the WIND commercial database and its industry classification for the construction sector.

their home countries ranging from a low of \$501.14 billion to a high of \$543.97 billion.<sup>314</sup> This market was relatively stable, with average annual change in total contracting revenues varying between 4% and 6% during this period.<sup>315</sup> Finally, while Mr. Chen and Mr. Wu discussed international markets in general terms in their speeches (such as the imperative of international competitiveness and the issue of declining overseas demand), they did not cite specific changes in international markets to justify their changes in organizational strategy or structure.

Ruling out these alternative explanations increases confidence in a political leadership explanation, but several caveats remain. First, while Mr. Chen and Mr. Wu reached top leadership posts after decades of work within the industry and their firms, the career trajectories that lead to leadership appointments in central state-owned enterprises vary and may reflect divergent motivations.<sup>316</sup> In addition, SASAC and State Council policies may affect central state-owned enterprises in different ways depending on the industries in which they operate and their historical relationships with the center. Finally, changes in international markets might impact even peer firms in the construction industry in varied ways, depending on the circumstances of the specific country markets in which they operate, or the state of industries like mining

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<sup>314</sup> The top 250 contractors are ranked on the basis of contracting revenues outside of their home countries. 2015 is the latest year for which data is available. Engineering News-Record “Top 250 International Contractors,” accessed on August 1, 2017 at <http://www.enr.com/toplists/2016-Top-250-International-Contractors>.

<sup>315</sup> Author’s calculations using Engineering News-Record data.

<sup>316</sup> Such motivations may include the Party center’s intention to broaden an individual’s experiences across functional areas of the Chinese bureaucracy as part of a grooming process for continued political advancement, efforts to foster organizational learning by bringing in individuals with successful experiences running other state firms, or attempts to limit the potential risk of departmentalism through intra-industry executive swaps. Departmentalism (本位主义, *benweizhuyi*) refers to a phenomenon in which long-serving individuals in specialized bureaucracies come to evaluate policy priorities from the perspective and interests of their own bureaucratic unit. Leutert forthcoming; Kenneth Lieberthal and Michel Oksenberg, *Policy Making in China: Leaders, Structures, and Processes* (Princeton, NJ: Princeton University Press, 1988).

and petroleum to which the infrastructure they specialize in constructing might be related (such as power plants). Further sector-specific and even company-specific research is needed in all three of these areas—personnel appointment, central policies, and market competition.

### ***Conclusion***

In this chapter, I have argued that political leadership is an important yet understudied factor shaping the economic reform of central state-owned enterprises in China. I investigated whether the political leadership that Mr. Chen and Mr. Wu exercised in China Building Company—their choices about strategies and organizational structure—impacted its economic reform. Specifically, I analyzed developments in three areas: changes in the level of marketization of global expansion efforts, shifts in influence among intra-firm entities, and how they conceptualize their relationship to international markets. I found that Mr. Chen’s bottom-up strategy of “prioritize the international, coordinate with the domestic” and changes to organizational structure resulted in market-oriented global expansion efforts, increased influence for market-oriented actors within the firm, and an organic binary conceptualization of intra-firm entities’ relationship to international markets. In contrast, Mr. Wu’s new strategy of “planning and design come first, technology leads,” and his creation of CBC International centralized global expansion efforts, increased influence for the holding company and other administrative actors within the firm, and an imposed tripartite conceptualization of intra-firm entities’ relationship to international markets. Table 3.3 below summarizes findings from the case study analysis.





Table 3.3: Summary of Mr. Chen and Mr. Wu's Chairmanships

|   | Mr. Chen   | Mr. Wu   |
|---|--|--|
| <b>Tenure</b>   | <ul style="list-style-type: none"> <li>• 2011-2015</li> </ul>  | <ul style="list-style-type: none"> <li>• 2015-Present</li> </ul>   |
| <b>Strategy</b>   | <ul style="list-style-type: none"> <li>• “Prioritize the international, coordinate with the domestic”</li> </ul>   | <ul style="list-style-type: none"> <li>• “Planning and design comes first, technology leads”</li> </ul>  |
| <b>Major changes to organizational structure</b>                  | <ul style="list-style-type: none"> <li>• Increase in the administrative rank of engineering bureaus</li> <li>• Authorization for engineering bureaus to conduct “autonomous marketing” overseas</li> </ul>   | <ul style="list-style-type: none"> <li>• Creation of CBC International</li> <li>• Withdrawal of engineering bureaus’ authorization to conduct “autonomous marketing” overseas</li> </ul>   |
| <b>Overseas expansion efforts</b>                                 | <ul style="list-style-type: none"> <li>• Market-oriented (decentralized): engineering bureaus play leading role</li> </ul>   | <ul style="list-style-type: none"> <li>• Administrative (centralized): holding company plays leading role</li> </ul>   |
| <b>Shifts in influence among intra-firm entities</b>              | <ul style="list-style-type: none"> <li>• Market-oriented engineering bureaus gain influence</li> <li>• Holding company supports increased market autonomy of engineering bureaus vis-à-vis Sino-Construction International, weakening its influence</li> </ul> | <ul style="list-style-type: none"> <li>• Administrative holding company gains influence</li> <li>• Holding company restrains market autonomy of engineering bureaus</li> <li>• Creation of CBC International further weakens influence of Sino-Construction International</li> </ul> |
| <b>Conceptualization of relationship to international markets</b> | <ul style="list-style-type: none"> <li>• Intra-firm entities develop conceptualization organically</li> <li>• Binary: ‘front party’ and ‘back party’</li> </ul>  | <ul style="list-style-type: none"> <li>• Administrative superiors impose modified conceptualization</li> <li>• Tripartite: ‘front party,’ ‘middle party,’ ‘back party’</li> </ul>  |

Additional empirical study is needed to assess whether this chapter's findings about political leadership's impact on economic reform at the company level can be extended to other state-owned enterprises in China and beyond. Further research could examine the effects of political leadership on economic reform for a group of Chinese state-owned enterprises in a single industry or across industries during a particular period. Alternatively, it could follow the approach here of examining multiple consecutive chairmanships in selected central state-owned enterprises over time. Additional research could also be comparative in nature. For instance, it might investigate the effects of state-owned enterprise heads' political leadership on economic reform in central versus local state-owned enterprises or in different sub-national regions. Alternatively, it could assess the impact of political leadership on state-owned enterprise reform in different country contexts or under different types of political regimes. Finally, future studies could also develop and assess alternative explanations beyond the three examined here: intervention by external actors, major changes in central-level policies, and fluctuations in market competition.

Future research about the impact of political leadership on Chinese state-owned enterprise reform could address four specific areas. First, the upper echelons literature in business studies suggests a possible relationship between central state-owned enterprises' economic reform and the individual attributes of their leaders.<sup>317</sup>

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<sup>317</sup> The 'upper echelons' literature in business studies examines the impact of specific demographic attributes of the top management team, such as age and education (taken as measurement proxies for psychological constructs like cognitive bases, perceptions, and values), on a range of organizational outcomes. Mason A. Carpenter, Marta A. Geletkanycz, and Wm. Gerard Sanders, "Upper Echelons Research Revisited: Antecedents, Elements, and Consequences of Top Management Team Composition," *Journal of Management* 30, no. 6 (2004): 749-778; Donald C. Hambrick and Phyllis A. Mason, "Upper Echelons: The Organization as a Reflection of Its Top Managers," *Academy of Management Review* 9, no. 2 (1984): 193-206.

For example, an increasing number of central state-owned enterprise heads in China hold master's degrees or doctoral degrees in business administration. Are these individuals more likely to increase the marketization of global expansion efforts or to empower market-oriented actors within their companies? Second, research on elite factions suggests that social networks, especially patronage ties, condition individual officials' autonomy and influence.<sup>318</sup> Are heads of central state-owned enterprises who assume leadership after decades within a company less likely to make major changes to organizational structure than an individual appointed from outside the company, for instance from a previous position in central or local government? Third, analysis of central state-owned enterprise leaders' political mobility reveals that a significant proportion are appointed to lead more than one central state-owned enterprise during their careers.<sup>319</sup> Do these individuals replicate their previous strategies and changes to organizational structure in the enterprises where they are next appointed? Finally, research on local political budget cycles in China suggests that officials are likely to increase government spending at strategically important points in their leadership tenure in order to increase their probability of political promotion.<sup>320</sup> Are central state-owned enterprise heads more likely to make major changes to organizational structure early in their leadership terms? These are only some of the important issues that future research could address.

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<sup>318</sup> Victor C. Shih, *Factions and Finance in China: Elite Conflict and Inflation* (New York: Cambridge University, 2008); Franziska Keller, "Networks of Power: An Informal Network among Chinese Communist Elites 1982-2007," APSA 2014 Annual Meeting Paper, accessed on August 1, 2017 at: SSRN: <https://ssrn.com/abstract=2454603>.

<sup>319</sup> Leutert forthcoming.

<sup>320</sup> Gang Guo, "China's Local Political Budget Cycles," *American Journal of Political Science* 53, no. 3 (2009): 621-632.

## Chapter 4

### **Political Leadership and Central State-owned Enterprise Mergers**

Economic reform in a state-owned economy is typically understood as the decrease of administrative control over resource allocation and decision-making, epitomized by partial or full privatization of state-owned assets and corporate governance development.<sup>321</sup> Accordingly, ownership and control rights have long been the two main issues in research on state-owned enterprise reform. Arguments for state ownership underscore the needs to address market failure, to limit externalities like pollution, and to provide public goods such as health care and defense.<sup>322</sup> Other studies contend that state ownership harms productivity, efficiency, and profitability, with some suggesting that state regulation combined with taxes and subsidies is a better alternative.<sup>323</sup> Those who approach state-owned enterprise reform from the perspective of control rights often focus on the agency problems that state ownership

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<sup>321</sup> This view follows Kornai 1986's classic definition of economic reform as the process of moving away from administrative control toward market coordination. Janos Kornai, "The Soft Budget Constraint," *Kyklos* 39, no. 1 (1986): 3-30.

<sup>322</sup> William L. Megginson and Jeffry M. Netter, "From State to Market: A Survey of Empirical Studies on Privatization," *Journal of Economic Literature* 39, no. 2 (2001): 321-389.

<sup>323</sup> Kathryn L. Dewenter and Paul H. Malatesta, "State-owned and Privately-owned Firms: An Empirical Analysis of Profitability, Leverage, and Labor Intensity," *The American Economic Review* 91, no. 1 (2001): 320-334; Isaac Ehrlich, Georges Gallais-Hamonno, Zhiqiang Liu, and Randall Lutter, "Productivity Growth and Firm Ownership: An Analytical and Empirical Investigation," *Journal of Political Economy* 102, no. 5 (1994): 1,006-1,038; Roman Frydman, Cheryl Gray, Marek Hessel, and Andrzej Rapaczynski, "When Does Privatization Work? The Impact of Private Ownership on Corporate Performance in the Transition Economies," *The Quarterly Journal of Economics* 114, no. 4 (1999): 1,153-1,191; World Bank (1995), *Bureaucrats in Business: The Economics and Politics of Government Ownership* (Oxford: Oxford University Press, 1999).

creates and how to address them through particular corporate governance arrangements.<sup>324</sup>

However, economic reform in China's state-owned economy is comprised of both government-directed restructuring of state-owned assets as well as the extension of decision-making authority to non-state actors through marketization of assets and corporate governance.<sup>325</sup> Government-directed restructuring of state-owned assets may contradict how some researchers understand the concept of "reform," because it involves the government intervening in resource allocation instead of granting markets a greater role. However, government-directed restructuring of state-owned assets is an essential part of how reform of the state-owned economy actually occurs and is understood in China. As Chinese economist Li Yining writes: "It is important to know that in China, the reorganization of state-owned assets is an indispensable part of the process of transition from a planned economic system to a market economy."<sup>326</sup> While a handful of empirical studies address the restructuring of state-owned assets in China, existing research remains limited and most works do not address developments during the past decade.<sup>327</sup>

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<sup>324</sup> Yingyi Qian, "Enterprise Reform in China: Agency Problems and Political Control," *Economics of Transition* 4, no. 2 (1996): 427-447; Xiaonian Xu and Yan Wang, "Ownership Structure and Corporate Governance in Chinese Stock Companies," *China Economic Review* 10, no. 1 (1999): 75-98.

<sup>325</sup> Vertical government-directed restructuring of state-owned assets refers to government bodies' deliberate organizational reforming (重组, *chongzu*) of state-owned enterprises through the consolidation, recombination, transfer, and/or sale of existing assets and of authority relations for their management.

<sup>326</sup> 厉以宁 [Li Yining], speech at the first Private Economy Forum at the Guanghua School of Management at Peking University, published in 《厉以宁改革论集》 [Collected Works of Li Yining on Reform] (Beijing: Zhongguo fazhan chubanshe, 2008): 186.

<sup>327</sup> Studies analyzing the extent of ownership restructuring and reassignment of property rights in state-owned enterprises include Jefferson and Singh 1998, Jefferson and Su 2005, Lin and Zhu 2001, and Steinfeld 1998. Keister 2000 and Sutherland 2003 examine the development of state-owned industrial enterprise groups. None of these studies addresses developments in the past decade. Gary H. Jefferson and Inderjit Singh, *Enterprise Reform in China: Ownership, Transition, and Performance* (New York:

At the central level, multiple reform efforts since 1978 have involved government restructuring of state-owned assets with the aim of developing large, internationally competitive state-owned conglomerates. Experimentation with ‘general companies’—large corporate entities under central ministries linking multiple factories across provincial lines—starting in 1981 was followed by central-level promotion of large industrial state-owned ‘enterprise groups’ beginning in 1991.<sup>328</sup> In 1998, reorganization of the State Council broke up existing ‘general companies’ into centrally-controlled enterprises along geographic or vertical industry lines. At each stage, the government actively directed the restructuring of state-owned assets and carried it out through an administrative process. While heads of state-owned enterprises had significant influence on the restructuring process at the enterprise level, the government exercised predominant authority to initiate or to approve large-scale mergers.

Since the establishment of the State-owned Assets Supervision and Administration Commission (SASAC) in 2003, government restructuring of state-owned assets has proceeded primarily through SASAC-directed mergers among central state-owned enterprises. Mergers include two main types of asset consolidation:

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Oxford University Press, 1998); Gary H. Jefferson and Jian Su, “Privatization and Restructuring in China: Evidence from Shareholding Ownership, 1995-2001,” *Journal of Comparative Economics* 34, no. 1 (2006): 146-166; Lisa A. Keister, *Chinese Business Groups: The Structure and Impact of Interfirm Relations during Economic Development* (Oxford University Press, 2000); Yi-min Lin and Tian Zhu, “Ownership Restructuring in Chinese State Industry: An Analysis of Evidence on Initial Organizational Changes,” *The China Quarterly* 166 (2001): 305-341; Edward S. Steinfeld, *Forging Reform in China: The Fate of State-owned Industry* (New York: Cambridge University Press, 1998); Dylan Sutherland, *China’s Large Enterprises and the Challenge of Late Industrialisation* (New York: Routledge, 2003).

<sup>328</sup> Enterprise groups differed from earlier experimentation with ‘general companies’ because they started from large production units (the core enterprises of the groups) at a lower level of the production system under central ministries, rather than originating from central ministry headquarters or even directly from the State Council itself. Li 2014: 64.

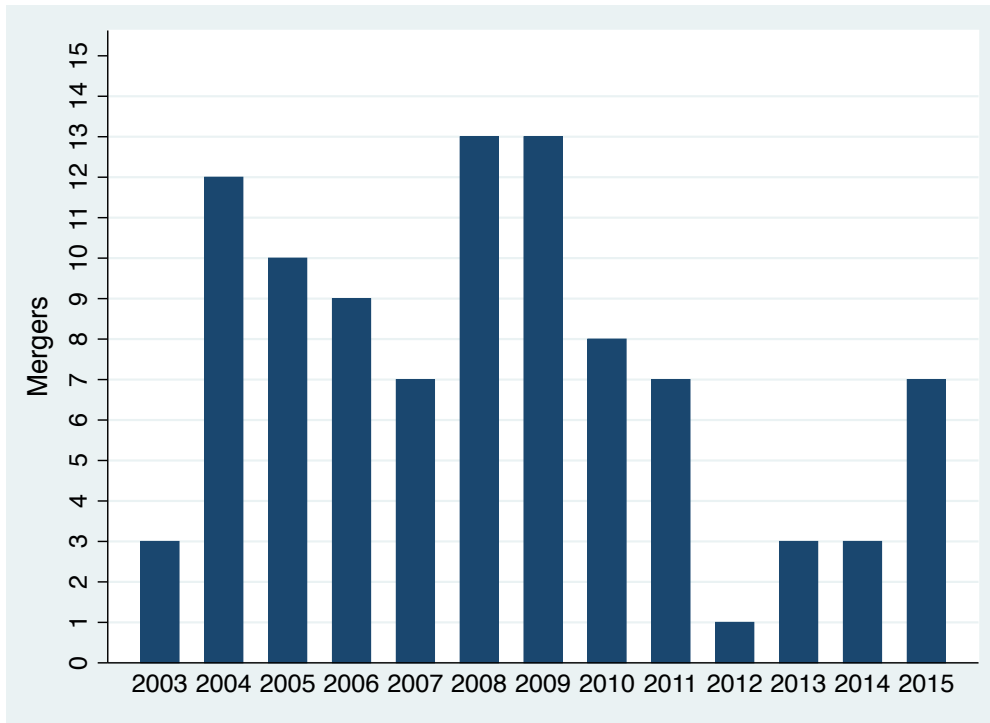
when a central state-owned company is merged into (并入, *bingru*) another state-owned company, or when two existing central state-owned enterprises are combined (合并, *hebing*) to create a new firm. Both economic and political factors motivate these mergers. In theory, they can boost competitiveness by eliminating price wars among central state-owned enterprises overseas, combining complementary capacities, and increasing resources—employees, capital, and client networks. In addition, mergers among central state-owned enterprises constitute a key method for restructuring and upgrading domestic industry. They enable coordinated cuts in surplus capacity industries, reduction of losses by merging poor performers into stronger firms, and price stabilization for products previously undervalued because of market competition among state firms. Consolidation of state-owned assets is also politically appealing. Most importantly, it avoids the sensitive issues of selling state firms, which prompts corruption concerns, or closing them and dismissing their employees, which raises the specter of social instability. It also fits the central leadership’s longstanding strategic vision for the development of China’s ‘national champions’—market competitiveness with Party control.

SASAC-directed mergers have steadily transformed the central government’s portfolio of state-owned enterprises since 2003. Between 2003 and 2015, 96 central state-owned enterprises under SASAC’s administration were merged. However, the incidence of mergers among central state-owned enterprises during this period has varied significantly across firms and over time (see Figure 4.1). This suggests that government-directed restructuring of central state-owned enterprises through mergers cannot simply be attributed to a developmental sequence in which asset consolidation



occurs early on and enterprises are stable once formed. What factors then affect the incidence of central state-owned enterprise mergers?

Figure 4.1: Central State-owned Enterprise Mergers, 2003-2015



In this chapter, I assess three hypotheses, drawn from existing research, for the incidence of mergers among central state-owned enterprises between 2003 and 2015. First, a top-level political leadership hypothesis posits that mergers should be most likely for central state-owned enterprises operating in sectors that the State Council has designated as of high strategic importance, as China’s leadership deliberately aims to concentrate state-owned assets in a small number of firms in the “commanding heights” of the economy. Second, a middle-level political leadership hypothesis suggests that mergers should be most frequent during the tenures of SASAC directors

whose reform strategies prioritize asset consolidation. Third, a market competition hypothesis posits that mergers should be most likely when market competition is high, as only the fittest firms survive and the government acts to protect state firms' market share and prevent price wars. I assess these hypotheses with logistic regression analysis on the likelihood of mergers using an extensive original dataset compiled from SASAC yearbooks, the WIND financial database, company websites, and media reports. I find strong support for the top-level political leadership hypothesis and little support for the middle-level political leadership and market competition hypotheses. These findings are robust to the inclusion of additional variables to capture the possible effects of central state-owned enterprise heads' previous work experience at the center.

## ***Hypotheses***

### *Top-level Political Leadership*

Strategic design accounts of China's economic reform underscore the importance of decisions by top national leaders about the particular industries in which state-owned assets are to be concentrated. As Roselyn Hsueh (2011) contends, these decisions proceed from assessments about the "perceived strategic value" of particular industries.<sup>329</sup> The government is more likely to centralize bureaucratic coordination, to regulate market entry, and to use industrial policy to target the development of sectors with high strategic importance. In contrast, the government is more likely to

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<sup>329</sup> Roselyn Hsueh, *China's Regulatory State: A New Strategy for Globalization* (Ithaca, NY: Cornell University Press, 2011); Roselyn Hsueh, "State Capitalism, Chinese-Style: Strategic Value of Sectors, Sectoral Characteristics, and Globalization," *Governance* 29 (2016): 85–102.

decentralize bureaucratic coordination and to deregulate market entry in sectors with less strategic importance. Official designation of industry strategic importance impacts the likelihood of government intervention to restructure specific sectors and the enterprises operating in them through consolidating, recombining, transferring, and/or selling existing assets.

The Jiang Zemin administration (1989-2002) initiated official designation of industry strategic importance in China. In Jiang's Report to the 15<sup>th</sup> National Party Congress in 1992, he emphasized that absolute state control of the economy was not necessary but rather its control of the “commanding heights” (国民经济命脉, *guomin jingji mingmai*)—specific sectors deemed critical to the national economy.<sup>330</sup> The Fourth Plenum in 1999 specified that state ownership should maintain the “dominant position” (支配地位, *zhipei diwei*) in “important industries and key areas” (重要行业和关键领域, *zhongyao hangye he guanjian lingyu*).<sup>331</sup> During the subsequent Hu Jintao administration, the State Council further differentiated and formalized the strategic importance of specific sectors in 2006 when it designated seven industries where the state will maintain “absolute control,” and nine industries where it will keep “strong control.”<sup>332</sup> These two groups, together with industries not designated as

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<sup>330</sup> Jiang Zemin, Report to the National Party Congress, October 12, 1992.

<sup>331</sup> It specified three important industries (sectors relating to national security, natural monopolies, and public goods or services provision) and one key area (high and emerging technology industries)—as well as “backbone enterprises in important industries” (重要产业中的骨干企业, *zhongyao chanye zhong de guban qiye*). Central Committee of the Communist Party of China: 《中共中央关于国有企业改革和发展若干重大问题的决定》 [The Decision of the Central Committee of the Communist Party of China on Major Issues Concerning the Reform and Development of State-Owned Enterprises], September 22, 1999.

<sup>332</sup> Industries where the state will keep “absolute control” are: defense, electricity, petroleum, telecommunications, coal, aviation, and shipping. Sectors where it will maintain “strong influence” are: machinery, electronics, information technology, automobiles, steel, nonferrous metals, chemicals, and

strategically important, comprise what Margaret Pearson (2015) terms China’s “tiered economy.”<sup>333</sup>

One observable implication of a top-level political leadership explanation is a positive relationship between the level of strategic importance of the industry to which a central state-owned enterprise belongs and the incidence of mergers. Specifically, mergers should be most likely for central state-owned enterprises in industries with high strategic importance, as the state deliberately seeks to concentrate state-owned assets in a small number of firms in specific sectors that it deems strategically important to China’s national economy. Table 4.1 below summarizes the levels of industry strategic importance in China according to the State Council’s 2006 classification scheme.

Table 4.1: Official Designation of Industry Strategic Importance in China

| Role for state     | Industries   | Official designation of strategic importance |
|--------------------|--|--|
| “absolute control” | Defense, electricity, petroleum, telecommunications, coal, aviation, shipping                                  | High   |
| “strong influence” | Machinery, electronics, information technology, automobiles, steel, nonferrous metals, chemicals, construction | Low  |
| None specified     | Investment, trade, research and development, services, agricultural products                                   | None specified                               |

construction. 《我国明确七大行业将由国有经济保持绝对控制力》 [China Specifies Seven Major Industries in Which the State-owned Economy Will Maintain Absolute Control], 《上海证券报》 [Shanghai Securities News], December 19, 2006.

<sup>333</sup> Margaret Pearson, “State-owned Business and Party-State Regulation in China’s Modern Political Economy,” *State Capitalism, Institutional Adaptation, and the Chinese Miracle*, eds., Barry Naughton and Kellee S. Tsai (New York: Cambridge University Press, 2015): 31-36.

**$H_1$ : Central state-owned enterprises in industries assigned higher levels of strategic importance are more likely to experience mergers.**

*Middle-level Political Leadership*

A middle-level political leadership explanation suggests that SASAC directors' exercise of political leadership may affect the likelihood of mergers among central state-owned enterprises.<sup>334</sup> SASAC directors exercise political leadership in two main ways. First, they set the specific strategies by which to achieve the center's goals: preserving and increasing the value of state assets, making central state-owned enterprises internationally competitive, and promoting the development of a modern enterprise system.<sup>335</sup> Second, SASAC directors can indirectly alter the organizational structures of the central state-owned enterprises under their administrative authority, for instance through consolidating or transferring assets among firms or mandating changes to their governance structures, such as the establishment of boards of directors. These two mechanisms of political leadership are complementary and SASAC directors often employ them in tandem. For example, a SASAC director might advance a reform strategy that emphasizes restructuring state-owned enterprises in a

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<sup>334</sup> I focus on SASAC directors rather than SASAC Party secretaries because they possess primary decision-making authority for setting reform strategies. Moreover, a single individual may jointly hold the positions of both director and Party secretary. For example, SASAC director Li Rongrong concurrently served as SASAC Party secretary between February 2005 and August 2010, as did his successor Wang Yong between August 2010 and March 2013.

<sup>335</sup> Development of a modern enterprise system refers primarily to the legal reorganization of state-owned enterprises as limited liability or shareholding companies and to corporate governance development.

particular way in order to increase the value of state-owned assets or to promote the development of a modern enterprise system.

Although SASAC directors exercise important decision-making authority for setting reform strategies and major organizational changes to central state-owned enterprises, they can only carry them out with the support and approval of their administrative superiors in the State Council and top national leaders. The autonomy granted to central state-owned enterprises themselves sets the bottom bound of SASAC directors' authority. SASAC directors can in theory influence the relative frequency by which mergers occur by setting reform strategies that place varying emphasis on asset consolidation; however, they are not directly involved in the logistics of particular mergers.<sup>336</sup> SASAC directors' relative scope for authority may also vary by issue area or under different political regimes.<sup>337</sup>

One observable implication of the middle-level political leadership hypothesis is a positive relationship between the extent to which a SASAC director's reform strategy emphasizes consolidation of state-owned assets and mergers. Specifically, we would expect that central state-owned enterprises are more likely to experience mergers when a SASAC director's reform strategy emphasizes consolidation of state-owned assets. The following sections analyze the emphasis that each SASAC

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<sup>336</sup> Within SASAC, the Enterprise Department (企业局, *qiye ju*) is responsible for the logistics of mergers among central state-owned enterprises.

<sup>337</sup> For example, SASAC directors do not typically determine the content or lead the execution of Party building/political education campaigns; the Central Organization Department determines campaign content and the Party secretary of SASAC is responsible for their implementation. Changes that particular regimes make to the hierarchy of organizations responsible for economic governance may also affect SASAC directors' space for political leadership (one example is the Xi Jinping administration's creation of the Central Leading Group for Comprehensively Deepening Reforms to centralize decision-making authority for economic reform).

director's reform strategy placed on consolidation of state-owned assets between 2003 and 2015.

The founding director of SASAC, Li Rongrong (August 2003-August 2010), emphasized the imperative of making central state-owned enterprises “large and strong” (做大做强, *zuo da zuo qiang*).<sup>338</sup> This reform strategy prioritized the consolidation of state-owned assets by making increased firm size the goal of reform. Mr. Li believed that asset consolidation could help to realize the center's objective of preserving and maintaining the value of state-owned assets in multiple ways. He felt that it could advance vertical industry integration and economies of scale within state-owned business groups, increase central state-owned enterprises' market share at home and abroad, and make central state-owned enterprises “strong” by amalgamating poor performers into stronger state firms.<sup>339</sup> At the very first meeting of central state-owned enterprise heads in December 2003, Mr. Li stated: “Facing the new situation of the quickening pace of global industrial restructuring and multinational corporations intensifying their global layout, we must enhance our sense of urgency and speed up the pace of enterprise reorganization and restructuring.”

The second director of SASAC, Wang Yong (August 2010-March 2013), did not prioritize state-owned asset consolidation. Instead, he stressed the importance of

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<sup>338</sup> Li Rongrong was formally appointed as SASAC director in March 2003; however, SASAC was not formally established until August 2003. Mr. Li also used the similar phrase of making central state-owned enterprises “strong and large” (做强做大, *zuo qiang zuo da*). Although at times the two phrases appear to be used interchangeably, he often used “strong and large” to refer to the need for enterprises to grow by performing well in their main business area, rather than to an overall reform strategy.

<sup>339</sup> Li Rongrong also pledged SASAC's support for central state-owned enterprises that met conditions to engage in overseas mergers and acquisitions; however, the primary focus remained domestic rather than international mergers. 李荣融 [Li Rongrong], 《重组必须有利于优势互补》 [Restructuring Must Be Beneficial to Complementing Mutual Strengths], 李荣融 [Li Rongrong], 《遵循规律办企业》 [Running Businesses Abiding by Rules] (Beijing: Zhongguo jingji chubanshe, 2013): 140.

making central state-owned enterprises “strong and excellent” (做强做优, *zuo qiang zuo you*). In an interview, Mr. Wang explained that his approach to making state firms “strong” entailed strengthening their innovation capacity, resource allocation ability, risk control and personnel quality, while making them “excellent” involved improving their operating performance, corporate governance, organizational layout, and social image.<sup>340</sup> This reform strategy deprioritized asset consolidation by removing “large” as a priority of reform strategy and focusing on company-level reforms, such as developing corporate governance, readjusting organizational structures, and improving operational efficiency.

After the short-lived tenure of SASAC director Jiang Jiemin (March 2013-August 2013), subsequent acting director and then director Zhang Yi (September 2013-January 2016) put the imperatives of fighting corruption and maintaining stability first and foremost.<sup>341</sup> Amalgamating his predecessors’ reform strategies, Mr. Zhang called for making central state-owned enterprises “strong, excellent, and large” (做强做优做大, *zuo qiang, zuo you, zuo da*).<sup>342</sup> However, although Mr. Zhang indicated renewed emphasis on consolidation of state-owned assets by again including firm size as a goal, he reordered the components of his reform strategy to put “making firms large” last. This indicated that although asset consolidation was again a component of Mr. Zhang’s reform strategy compared to that of his predecessor Mr.

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<sup>340</sup> 李其彦 [Li Qiyang], 鲁菲 [Lu Fei], 《国资委主任王勇: “做强做优”央企需制度保障》 [SASAC Director Wang Yong: “Strong and Excellent” Central State-owned Enterprises Need Institutional Guarantee], 《财经国家周刊》 [Economy and Nation Weekly], January 11, 2012.

<sup>341</sup> 《张毅接掌国资委:张老纪检”面临改革新任务》 [Zhang Yi Takes Over At SASAC: “Old Discipline Inspector Zhang” Faces New Reform Task], 《人民网—中国共产党新闻网》 [People’s Network CCP News Network], December 26, 2013.

<sup>342</sup> 《国资委 2015 年重点工作:全力以赴保增长居首位》 [SASAC 2015 Priority Work: Going All Out To Maintain Growth Takes First Place], 国资委网站 [SASAC Website], December 22, 2014.



Wang, it was still less of a priority than it had been in Mr. Li's reform strategy. In summary, this analysis of the SASAC directors' reform strategies suggests that mergers should be most likely during the tenure of Mr. Li and least likely during the tenure of Mr. Wang.

**$H_2$ : Central state-owned enterprises are more likely to experience mergers when the SASAC director's reform strategy emphasizes consolidation of state-owned assets.**

#### *Market Competition*

A third explanation derived from organic transformation accounts emphasizes adaptation to dynamic external conditions. It suggests that government-directed organizational restructuring of central state-owned enterprises is best understood as a response to changes in market competition. Rising market competition in a particular industry puts pressure on state firms to compete with one other and private companies—both domestic and international—through increasing operational efficiency, cutting costs, lowering prices, and improving product quality. The stability and improvement of state-owned enterprise performance matters to the government because state firm revenues and taxes constitute an important source of fiscal revenue. In cases where central state-owned enterprises struggle to compete or where making state firms bigger might boost their performance by promoting economies of scale or vertical industry integration, the government may therefore elect to restructure state firms. Combining central state-owned enterprises can help to maintain their

competitiveness and protect their industry position, thereby also ensuring the government's fiscal revenues.

Government-directed restructuring of state-owned enterprises in response to changing market conditions first became a major component of the government's strategy for state sector reform during the 1990s. The Fourth Plenum in 1995 officially endorsed "strategic reorganization" (战略性改组, *zhanluexing gaizu*) of the state-owned economy, to proceed "in accordance with the market and industrial policies."<sup>343</sup> Continued deterioration in the state sector's performance together with Chinese leaders' concern about rising domestic market competition after China's accession to the World Trade Organization (WTO) were early market motivations for government-directed restructuring of state-owned assets, including mergers.<sup>344</sup> Widespread and to some extent organic consolidation of state-owned assets at the local level occurred during the massive downsizing of the state sector under the strategy of "grasping the large, releasing the small." In the simultaneous consolidation of state-owned assets at the central level, the government took the lead in decisions about organizational restructuring—but it often invoked considerations about market competitiveness as it did so. For example, in a 2002 speech following China's accession to the World Trade Organization, Jiang Zemin emphasized both market opportunity and challenges as key

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<sup>343</sup> Central Committee of the Communist Party of China: 《中共中央关于制定国民经济和社会发展“九五”计划和 2010 年远景目标的建议》 [Suggestions of the Central Committee of the Communist Party of China on Formulating the 9<sup>th</sup> Five Year Plan for National Economic and Social Development and 2010 Long-Term Goals], September 28, 1995.

<sup>344</sup> In March 1999, the State Economic and Trade Commission reported that 30% of 7,680 large and medium state-owned enterprises were operating at a loss and one third of the 512 key large state-owned enterprises made losses during the first half of 1998. Moreover, state-owned companies accounted for an estimated 90% of all non-performing loans held by state-owned banks by 1999. China Statistical Yearbook.

factors motivating the development of a small group of large state-owned enterprise groups.<sup>345</sup>

An observable implication of a market competition explanation is a positive correlation between levels of market competition and the likelihood of mergers. Mergers should be more likely for central state-owned enterprises operating in industries with higher levels of market competition. This is because market competition erodes state firms' market share and puts pressure on them to lower prices. However, state-owned enterprises are limited in their ability to adapt to market pressures since mass layoffs are not politically acceptable.<sup>346</sup> Moreover, state firms are also expected to fulfill political priorities that contradict profit maximization.<sup>347</sup> Government-directed organizational restructuring therefore may be one possible method by which adjustment to changes in market competition occurs. Increased industry competitiveness should thus ultimately lead to survival of central state-owned enterprises that the government deems fittest, not the survival of all.

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<sup>345</sup> Jiang stated: "In the long run, we must form a group of internationally competitive large enterprises and multinational enterprises. We must seize all opportunities under the new situation after joining the WTO and strive to form and develop a group of Chinese-style multinational companies. Our expansion of opening up, increase in economic strength and international competitiveness, and withstanding of the various challenges of economic globalization are urgently needed in order for China to truly become an economic great power." 《中共中央总书记、国家主席、中央军委主席江泽民出席省部级主要领导干部“国际形势与世贸组织”专题研究班座谈会并发表重要讲话》 [General Secretary of the CCP, National Chairman, and Chairman of the Central Military Commission Jiang Zemin Attended the "International Situation and the World Trade Organization" Symposium for Main Leading Cadres at the Provincial Level and Delivered an Important Speech], 《新华社》 [Xinhua News], February 25, 2002.

<sup>346</sup> Recent comments by SASAC director Xiao Yaqing at the National People's Congress in March 2017, in which he emphasized that reform of central state-owned enterprises would absolutely not generate a "wave of layoffs," reflect the political sensitivity of mass layoffs. 《肖亚庆:央企改革绝对不会出现什么“下岗潮”》 [Xiao Yaqing: Central State-owned Enterprise Reform Absolutely Will Not Bring Any Appearance of "Wave of Layoffs"], 《中国证券网》 [China Securities Network], March 9, 2017.

<sup>347</sup> These political priorities include fostering indigenous innovation, supporting social stability and crisis response in China, and advancing economic initiatives abroad such as the Xi Jinping administration's "One Belt, One Road" initiative.

**$H_3$ : Higher levels of market competition in the domestic industries in which central state-owned enterprises operate increase the likelihood of mergers.**

I test these hypotheses using data about industry market competition and the attributes and mergers of all central state-owned enterprises in China between 2003 and 2015.

The following section introduces the sample, variables, data sources, and coding procedures used.

### ***Variables and Data***

#### ***Sample***

The sample includes the 189 non-financial central state-owned enterprises under SASAC's administration at its founding in 2003.<sup>348</sup> These firms represent the universe of cases of central state-owned enterprises. I include the new firms created through mergers (合并, *hebing*) in the dataset as separate observations because of the possibility that one firm may experience multiple mergers. In the few cases where a new central state-owned enterprise was set up (组建, *zujian*) after 2003, I add them into the dataset into their year of creation. When a given firm is merged into and absorbed by another firm (并入, *bingru*) or combined with another firm to form a new entity (合并, *hebing*), its firm-year observations end the year that the merger is approved and it is removed from the dataset. The data range from 2003 to 2015,

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<sup>348</sup> The starting point of the analysis is the official list of 189 central state-owned enterprises under SASAC's administration at its establishment in 2003. For this list, see State Council: 《国务院办公厅关于公布国务院国有资产监督管理委员会履行出资人职责企业名单的通知》 [General Office of the State Council Notice Regarding the State-owned Assets Supervision and Administration Commission Carrying Out Investor Responsibilities Enterprise List], October 21, 2003.

yielding an unbalanced panel dataset with 1,901 firm-year observations. Additional data sampling and analysis is needed to assess whether this study's findings can be extended to other cases, such as state-owned enterprises owned by governments in China below the central level.

### *Dependent Variable*

The dependent variable for this study is the incidence of central state-owned enterprise mergers, measured at the company level by year (0 for no merger, 1 for merger). A merger occurs if a central state-owned enterprise is either merged into another existing central state-owned enterprise or if it is combined with another existing central state-owned enterprise to form a new firm in a given year. Central state-owned enterprises refer to those firms under the administration of SASAC. Data on mergers were collected from SASAC's official website ([www.sasac.gov.cn](http://www.sasac.gov.cn)), company websites, and media reports.<sup>349</sup>

### *Independent Variables*

I evaluate top-level political leadership by examining the Chinese leadership's designation of industry strategic importance. To assess the varying strategic importance of particular sectors, I use the State Council's official listing in 2006 of seven industries in which the state is to maintain "absolute control" and nine industries in which the state is to keep "strong influence," as this remains the most recent official

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<sup>349</sup> See Appendix B for a list of all central state-owned enterprises that experienced mergers and the firms into which they were either merged with or combined to create new firms between 2003 and 2015.

designation of industry strategic importance (see Table 4.1 above).<sup>350</sup> I first use SASAC's industry classification scheme to identify the sector to which a central state-owned enterprise belongs, and then use the State Council's 2006 official listing to categorize it as operating in an industry of high strategic importance (where the state is to maintain "absolute control"), an industry of low strategic importance (where the state is to keep "strong influence"), or an industry that is not formally designated as possessing strategic importance (all other sectors). I use these measures to create a categorical variable with values ranging from 0 (no official designation of strategic importance) to 2 (high strategic importance).

I examine middle-level political leadership by looking at SASAC directors and the relative emphasis that their reform strategies place on the consolidation of state-owned assets. I identify SASAC directors' reform strategies from their speeches and writings, reports on SASAC's official website, Chinese media reports, and secondary sources.<sup>351</sup> Over the study period, there are three different directors: Li Rongrong (2003-2010), Wang Yong (2011-2013), and Zhang Yi (2014-2015).<sup>352</sup> Based on my textual analysis of their reform strategies, Wang Yong emphasizes asset consolidation the least, Li Rongrong stresses asset consolidation the most, and Zhang Yi falls in between the two. Each variable takes the value of 1 for years during that SASAC

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<sup>350</sup> I assume that the varying levels of strategic importance assigned to these industries already existed in 2003, even though the State Council did not formally codify them until 2006.

<sup>351</sup> It is important to note that SASAC directors typically articulate strategies for reform within approximately one year of taking office; this increases confidence that reform strategies precede and can therefore be theorized to shape behavior and are not merely a post-hoc rationalization of actions that have already occurred.

<sup>352</sup> I code the year of 2013 as part of Wang Yong's leadership tenure because due to the brevity of Jiang Jiemin's directorship (March-August 2013) and because he was under investigation for corruption from the start of his time at SASAC, it is reasonable to assume that any mergers that occurred during his tenure resulted from planning that had already been initiated during Wang Yong's leadership.

director's tenure and 0 otherwise. I expect more mergers under Li Rongrong than under other SASAC directors. This measurement assumes that each SASAC director's reform strategy is in effect for the duration of his tenure, which is a reasonable assumption, while also controlling for other idiosyncratic influences that SASAC directors' leadership tenure may have on the likelihood of mergers.

I assess market competition by measuring the relative proportion of state-owned enterprises among all firms operating in a particular industry in China. I calculate this based on the ratio of publicly listed companies in a given industry on both the Shenzhen and Shanghai stock markets for which the ultimate parent company is a state-owned enterprise. This proportion varies over time with changes in the numbers of state-owned and private companies active in a particular industry. As a single central state-owned enterprise may have multiple publicly listed subsidiaries operating in different industries, I classify its industry based on the WIND industry classification for its largest publicly listed subsidiary company (by asset size). For central state-owned enterprises that do not have publicly listed subsidiaries, I classify them according to the WIND industry classification that corresponds to their main business area (主业, *zhuye*). I calculate the proportion of state-owned enterprises compared to privately-owned enterprises in a given industry by year. Market competition is a continuous variable with values ranging from 0 to 1; increasing values indicate a greater proportion of private companies in an industry market and higher levels of competition. Table 4.2 below summarizes the independent variables used in the analysis and their expected signs.

Table 4.2: Independent Variables and Expected Coefficient Signs

| <b>Variable</b>                          | <b>Sign</b> |
|--|-------------|
| <i>Top-level political leadership</i>    |             |
| Industry strategic importance            | +           |
| <i>Middle-level political leadership</i> |             |
| SASAC director reform strategy           | +           |
| <i>Market competition</i>                |             |
| Level of domestic industry competition   | +           |

### *Control Variables*

To better isolate the impact of these independent variables of interest, I also include a series of control variables. First, I include a control variable for central state-owned enterprise size based on total assets.<sup>353</sup> Large firm size may decrease the likelihood that a central state-owned enterprise is merged, because the government may be less likely to alter the organizational structure of major industry players due to potential market disruption and logistical difficulties. In contrast, smaller central state-owned enterprises may be more likely to be merged into larger state firms, which might hold advantages in market share, production capacity, and/or technological capabilities. To calculate firm size, I first average the total reported assets for the central state-owned enterprises in the years for which this data is given in SASAC's annual yearbooks to calculate three size cut points—small, medium, and large. Using these cut points, I then classify the size of each central state-owned enterprise according to the SASAC yearbook data or the most recent reported data on total asset size from company

<sup>353</sup> While it might appear that size and strategic value could be highly correlated, Variance Inflation Factor (VIF) tests do not indicate significant collinearity (VIF < 10).



websites, the SASAC website, and official Chinese media to categorize the size of the remaining state firms.<sup>354</sup> I code size as a categorical variable with values ranging from 1 (small) to 3 (large).

I also include a control variable for central state-owned enterprises' administrative rank. Central state-owned enterprises are divided into two main groups. The first is a core set of state firms termed "important backbone state-owned enterprises" (重要骨干国有企业, *zhongyao guban guoyou qiye*) which are ranked at the vice-ministerial level (副部级, *fubuji*).<sup>355</sup> The remaining group of central state-owned enterprises are ranked at the department level (正厅级, *zhengtingji*). Central state-owned enterprises with vice-ministerial rank are typically larger in size than firms ranked at the department level but vary significantly with regard to the strategic importance of the sectors in which they operate.<sup>356</sup> Vice-ministerial ranked firms may be less likely to experience mergers than lower-ranked firms due to their status as the "core" of the state-owned economy; moreover, their greater influence and relatively larger size increase the political and logistical challenges of mergers. I create a binary variable that takes the value of 1 if a company possesses vice-ministerial rank and 0 otherwise.

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<sup>354</sup> A list of firms for which SASAC yearbooks did not report information on total assets and data sources other than SASAC yearbooks were used to code firm size is available from the author upon request.

<sup>355</sup> For a recent list of these firms, see Kjeld Erik Brødsgaard, "Politics and Business Group Formation in China: The Party in Control?" *The China Quarterly* 211 (2012): 635-637. The members of this group have remained largely constant over time, with only slight changes as mergers have reduced the number of firms and several new central state-owned enterprises created after 2003 were also accorded 'core' firm status, such as China Commercial Aircraft Group Corporation (中国商用飞机集团公司) and National Nuclear Power Technology Company, Ltd. (国家核电技术有限公司).

<sup>356</sup> Administrative rank is positively correlated with firm size and strategic value; however, Variance Inflation Factor (VIF) tests do not indicate any significant collinearity ( $VIF < 10$ ). Hosmer and Lemeshow goodness of fit tests also indicate that models including administrative rank as a control variable fit the data better than those without it.

I also include a control variable to indicate whether a central state-owned enterprise is a research or design institute. Research institutes (研究院, *yanjiuyuan*) and design institutes (设计院, *shejiyuan*) differ from other types of central state-owned enterprises because their primary function is to conduct activities related to research and development, although they may also engage in production indirectly by providing services such as consulting for technical designs or even directly by operating for-profit subsidiaries. Research institutes and design institutes may be more likely to experience mergers than other types of central state-owned enterprises, because the combination of research and design expertise with production capacity has long been a main objective of state-owned asset consolidation. I identify research and design institutes using the “research and design” (科研设计, *keyuan sheji*) official industry classification assigned by SASAC. The variable takes the value of 1 if a central state-owned enterprise is a research or design institute and 0 otherwise.

Finally, I include a control variable corresponding to the pre- and post- global financial crisis periods.<sup>357</sup> The global financial crisis reached worldwide proportions by 2008 with the collapse of Lehman Brothers in the United States. In that year, the Chinese government announced a ¥4 trillion (approximately \$590 billion) stimulus package to address the effects of the crisis on China’s domestic economy.<sup>358</sup> The external shock of the global financial crisis can be considered a dividing line in the

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<sup>357</sup> I include this theoretically informed variable to control for possible time effects instead of year fixed effects for two reasons. First, the inclusion of time dummies to control for possible year-variant time effects is confounded with the temporal variation implicit in the independent variable of SASAC directors’ reform strategies, because these reform strategies correspond to a given director’s leadership tenure. Second, no prior theoretical explanation exists in this case for why one would expect year-variant time effects.

<sup>358</sup> Barry Naughton, “Understanding the Chinese Stimulus Package,” *China Leadership Monitor* 28, no. 2 (2009): 1-12.

landscape of state-owned enterprise reform in China, because it affirmed the Chinese government's desire for greater autonomy through the accelerated development of a select group of "national champions"—large, internationally competitive state-owned companies.<sup>359</sup> At the same time, the increased amount of loans and credit that the stimulus package channeled to state-owned enterprises provided complementary material support for this aspiration.<sup>360</sup> I create a binary variable that takes the value of 0 in the pre-global financial crisis period (2003-2007) and 1 in the post-global financial crisis period (2008-2015). Below, Table 4.3 reviews the control variables used in the analysis and their expected signs; Table 4.4 provides summary statistics for all variables.

Table 4.3: Control Variables and Expected Coefficient Signs

| <b>Variable</b>              | <b>Sign</b> |
|------------------------------|-------------|
| Size (total assets)          | -           |
| Vice-ministerial rank        | -           |
| Research institute           | -           |
| Post-global financial crisis | +           |

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<sup>359</sup> For a discussion of how the global financial crisis increased the Chinese government's desire for greater autonomy in the realms of currency and the global monetary order, see Jonathan Kirshner, "China, Regional Hegemony, and an Emerging RMB Zone," *The Great Wall of Money: Politics and Power in China's International Monetary Relations* (Ithaca, NY: Cornell University Press, 2014).

<sup>360</sup> According to a 2017 report by Gavekal Dragonomics: "SOEs [state-owned enterprises] have consistently accounted for 70-80% of infrastructure investment in recent years. An infrastructure stimulus is by definition an SOE stimulus, and the central government has repeatedly used public works spending to stimulate the economy since 2008." Gavekal Dragonomics, "The State of the State Sector," March 2017.

Table 4.4: Summary Statistics

| Variable   | Mean  | Standard deviation | Min. | Max. | n     |
|--|-------|--------------------|------|------|-------|
| Merger   | 0.050 | 0.219              | 0    | 1    | 1,901 |
| Industry strategic importance<br>(top-level political leadership)        | 1.965 | 0.806              | 1    | 3    | 1,901 |
| SASAC director tenure—Li Rongrong<br>(middle-level political leadership) | .692  | .462               | 0    | 1    | 1,901 |
| SASAC director tenure—Wang Yong<br>(middle-level political leadership)   | .189  | .392               | 0    | 1    | 1,901 |
| SASAC director tenure—Zhang Yi<br>(middle-level political leadership)    | .119  | .323               | 0    | 1    | 1,901 |
| Market competition   | 0.630 | 0.324              | 0    | .993 | 1,901 |
| Size   | 2.153 | 0.799              | 1    | 3    | 1,844 |
| Research institute   | 0.075 | 0.263              | 0    | 1    | 1,901 |
| Vice-ministerial rank  | 0.348 | 0.476              | 0    | 1    | 1,901 |
| Post-global financial crisis period                                      | 0.534 | 0.499              | 0    | 1    | 1,901 |

### ***Research Design and Results***

I compute maximum likelihood estimates for a binary logistic regression with robust standard errors clustered by firm ID. I analyze a total of 1,901 firm-year observations for all Chinese central state-owned enterprises between 2003 and 2015. I estimate a series of models with results reported in Table 4.5 below. Model 1 assesses the effects of top-level political leadership (top national leaders and State Council), plus control variables. Model 2 assesses the effects of middle-level political leadership (SASAC directors), plus control variables. Model 3 examines the effects of market competition, plus control variables. Model 4, the full model, assesses the effects of top-level and middle-level political leadership and market competition, plus control variables.

Table 4.5: Estimation Results for Logistic Regression Models

| Variable                      | Model 1             | Model 2             | Model 3             | Model 4             |
|-------------------------------|---------------------|---------------------|---------------------|---------------------|
| Industry strategic importance |                     |                     |                     |                     |
| Low                           | 0.668*<br>(0.317)   |                     |                     | 0.683*<br>(0.311)   |
| High                          | 1.356**<br>(0.283)  |                     |                     | 1.340**<br>(0.279)  |
| SASAC director Li Rongrong    |                     | 0.184<br>(0.375)    |                     | 0.106<br>(0.378)    |
| SASAC director Wang Yong      |                     | -0.466<br>(0.452)   |                     | -0.477<br>(0.45)    |
| Market competition            |                     |                     | -0.158<br>(0.364)   | -0.16<br>(0.325)    |
| Size (medium)                 | -1.258**<br>(0.28)  | -0.946**<br>(0.261) | -0.978**<br>(0.267) | -1.230**<br>(0.278) |
| Size (large)                  | -2.379**<br>(0.555) | -1.851**<br>(0.48)  | -1.908**<br>(0.494) | -2.325**<br>(0.54)  |
| Vice-ministerial rank         | -1.115*<br>(0.536)  | -0.882<br>(0.521)   | -0.875<br>(0.522)   | -1.127*<br>(0.536)  |
| Research institute            | -0.828<br>(0.501)   | -0.546<br>(0.434)   | -0.567<br>(0.443)   | -0.829<br>(0.493)   |
| Post-global financial crisis  | 0.735**<br>(0.268)  | 0.808**<br>(0.271)  | 0.624*<br>(0.267)   | 0.932**<br>(0.289)  |
| Constant                      | -2.810**<br>(0.238) | -2.557**<br>(0.434) | -2.273**<br>(0.259) | -2.838**<br>(0.485) |
| AIC                           | .332                | 0.339               | 0.340               | 0.333               |
| BIC                           | -13,210.557         | -13,196.118         | -13,200.496         | -13,190.988         |
| Observations                  | 1,844               | 1,844               | 1,844               | 1,844               |

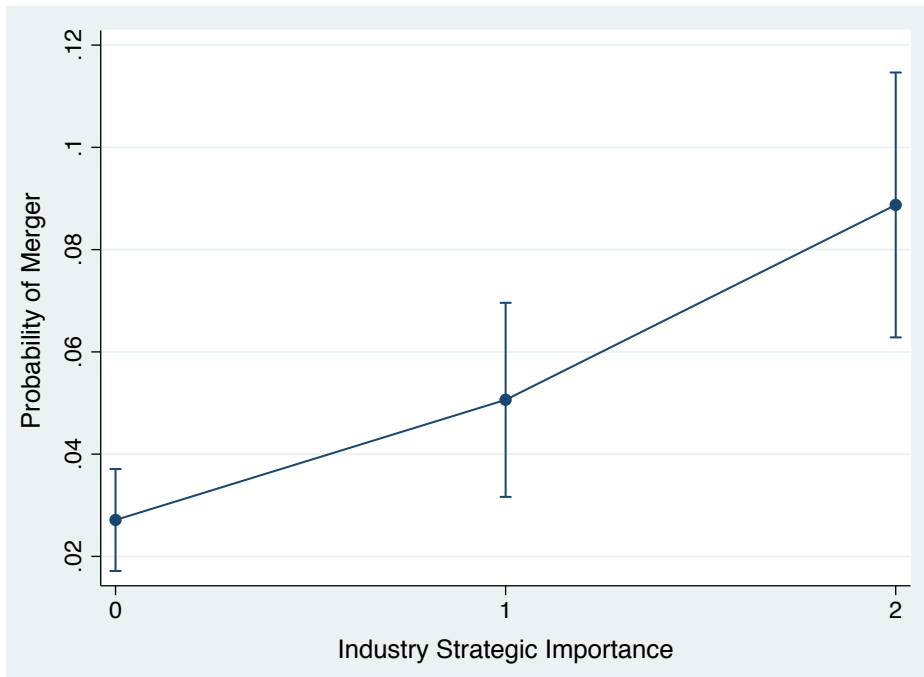
Robust standard errors in parentheses

\*\* p&lt;0.01, \* p&lt;0.05

The top-level political leadership hypothesis suggests that higher levels of industry strategic importance assigned by the State Council increase the likelihood of mergers. Model 1 assesses the effects of top-level political leadership (top national leaders and State Council), plus control variables. Results presented in Table 4.5 (columns 1 and 4) strongly support this hypothesis. The likelihood of mergers increases relative to the strategic importance of the industry in which a central state-owned enterprise operates. This positive relationship is consistent and is statistically significant across all of the models.

Based on the full model (column 4), the predicted probability of merger for central state-owned enterprises operating in a sector with no formal designation of strategic importance (strategic importance = 0) is .027, for those operating in a sector where the state is to retain “strong influence” (strategic importance = 1) the predicted probability of merger is .051, and for those operating in a sector where the state is to retain “absolute control” (strategic importance = 2) the predicted probability of merger is .089, holding all other variables at their means. Figure 4.2 below shows that the predicted probability of merger grows as industry strategic importance increases and that this positive relationship is consistent across all levels of industry strategic importance. The confidence intervals shown indicate the precision of these estimates of predicted probability of merger at each level of industry strategic importance.

Figure 4.2: Predicted Probability of Merger by Industry Strategic Importance with 95% Confidence Intervals (Top-Level Political Leadership)



The positive and statistically significant relationship between industry strategic importance and mergers accords with the Chinese government’s deliberate efforts since the 1990s under Jiang Zemin’s leadership to concentrate state ownership in specific sectors deemed critical to the national economy. This finding suggests that central state-owned enterprises are not merged indiscriminately; instead, mergers do aim at the consolidation of state-owned assets in the “commanding heights” of the state-owned economy.

Next, the middle-level political leadership hypothesis posits that greater emphasis on consolidation of state-owned assets in a SASAC director’s reform strategy increases the likelihood of central state-owned enterprise mergers. Model 2 assesses the effects of middle-level political leadership (SASAC directors), plus

control variables. Mergers should be least likely during the tenure of a SASAC director whose reform strategy does not prioritize asset consolidation (Wang Yong tenure = 1) and most likely during the tenure of a SASAC director whose reform strategy prioritizes asset consolidation (Li Rongrong tenure = 1). Results presented in Table 4.5 (column 2 and column 4) provide limited support for this hypothesis. Emphasis on consolidation of state-owned assets in SASAC directors' reform strategies is positively correlated with mergers across all of the models; however, this relationship is not statistically significant.

Finally, the market competition hypothesis suggests that higher levels of domestic competition in the sectors in which central state-owned enterprises operate increase the likelihood of mergers. Model 3 examines the effects of market competition, plus control variables. Results presented in Table 4.5 (column 3 and column 4) do not support this hypothesis. The correlation between market competition and mergers is negative and is not statistically significant in any of the models.

In addition, the results presented in Table 4.5 show a negative and statistically significant relationship between two other company-level variables—size and vice-ministerial rank—and the likelihood of mergers. The larger a company is in terms of asset size, the less likely it is to experience a merger. The negative relationship between size and mergers holds and is statistically significant across all of the models. In the full model, the predicted probability of merger for the smallest firms (size = 1) is .112, for medium-size firms (size = 2) the predicted probability of merger is .037, and for the largest firms (size = 3) the predicted probability of merger is .013, holding all other variables at their means. This finding is not surprising, because the largest



central state-owned enterprises often function as “merger recipients,” into which other central state-owned enterprises are amalgamated. State firms with vice-ministerial rank are also less likely to experience mergers. The negative relationship between vice-ministerial rank and mergers is consistent across all of the models. In the full model, the predicted probability of merger for firms that do not possess vice-ministerial rank (vice-ministerial rank = 0) is .053 and for firms with vice-ministerial rank (vice-ministerial rank = 1) the predicted probability of merger is .018, holding all other variables at their means. These findings further support the notion that mergers among central state-owned enterprises do not occur indiscriminately, nor primarily in response to market forces. Instead, they reflect a political design crafted by top-level leaders aimed at building a core group of large central state-owned enterprises concentrated in strategically important industries.

Finally, the results presented in Table 4.5 also indicate that mergers of central state-owned enterprises are more likely in the post-global financial crisis period. The positive and statistically significant relationship between the post-global financial crisis period and mergers holds across all of the models. Prior to the global financial crisis (before 2008, post-global financial crisis = 0), the predicted probability of merger estimated in the full model is .029; following the global financial crisis (2008 and after, post-global financial crisis = 1), the predicted probability of merger is .068, holding all other variables at their means. This finding too is consonant with a top-level political leadership explanation in which a predominantly political rather than economic logic drives mergers among central state-owned enterprises. This appears especially the case because China’s massive stimulus package in theory created an

economic environment in which central state-owned enterprises could both survive and grow larger—through infrastructure spending and easy credit at home and state-supported mergers and acquisitions abroad—without government-orchestrated mergers.<sup>361</sup>

### ***Robustness Checks***

One might also suggest that the professional backgrounds of central state-owned enterprise heads could be related systematically to the likelihood of mergers.<sup>362</sup>

Although these individuals do not have authority to decide whether mergers among central state-owned enterprises will occur, previous work experience in central government may make central state-owned enterprise heads more likely to implement the policies or decisions mandated by their administrative superiors. First, those with central government work experience may be more sympathetic to central directives and therefore more likely to carry them out, instead of seeking to delay or to resist them.<sup>363</sup> Second, individuals with central government work experience may be more likely to carry out mergers because they view them as less of a threat to their professional and personal interests than individuals who have spent their entire careers

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<sup>361</sup> The Xi Jinping administration (2012 to present) has justified ongoing mergers among central state-owned enterprises on economic grounds, by suggesting that mergers are intended to reduce excess domestic capacity (in sectors like steel, heavy machinery, and construction) produced by China's stimulus package and slowing domestic growth. However, it remains to be seen whether these mergers actually result in significant capacity cuts.

<sup>362</sup> I consider the chairman (董事长, *dongshizhang*) of a central state-owned enterprise to be its head. If a central state-owned enterprise does not have a board of directors, I consider the general manager (总经理, *zongjingli*) to be its head. It is possible for a single individual to concurrently hold more than one of the top three leadership positions in a central state-owned enterprise: board chairman, general manager, and Party secretary.

<sup>363</sup> Central government work experience is a standard measure for assessing officials' closeness to the center and their relative support for central policies. Yasheng Huang, *Inflation and Investment Controls in China: The Political Economy of Central-Local Relations during the Reform Era* (Cambridge: Cambridge University Press, 1999); Yumin Sheng, *Economic Openness and Territorial Politics in China* (Cambridge: Cambridge University Press, 2010).

working in state-owned industry or even a particular state firm. This is because time spent working in the central government may enable officials to develop broad knowledge and skills across functional areas and to cultivate informal connections at the center, both of which constitute important sources of comparative advantage in the competition for political promotion. Therefore, I expect that previous work experience at the center will increase the likelihood of central state-owned enterprise mergers.

To investigate this, I create a new variable measuring whether central state-owned enterprise heads have worked previously in the central government. For every firm-year observation, I first identify the head of each firm during that year and then assess whether he had previous work experience in a government or Party organ at the center, such as a State Council ministry or a central-level regulatory agency.<sup>364</sup> Data for this variable comes from an extensive original dataset on the biographical attributes of all central state-owned enterprise heads covering the period 2003 to 2015.<sup>365</sup> I compiled this dataset using their official CVs available online and Chinese media reports, as well as the Chinese Political Elites Database hosted by National Chengchi University.<sup>366</sup> I code this variable as 1 if the head of a central state-owned enterprise in a given year has previous central government work experience and 0 if he does not.<sup>367</sup> Out of 1,781 firm-year observations for which data on this variable is available, approximately 20% represent central state-owned enterprise heads with

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<sup>364</sup> I do not consider work in research institutes affiliated with ministries to be central government work experience.

<sup>365</sup> The dataset also includes information about central state-owned enterprise heads' previous local government work experience, age, highest educational attainment, and graduate degrees in business studies. None of these variables has a statistically significant relationship with the likelihood of mergers.

<sup>366</sup> 《中共政治精英资料库》[Chinese Political Elites Database], accessible at <http://cped.nccu.edu.tw/>.

<sup>367</sup> I use a binary measure here in order to maximize the number of observations for estimation, because some of the official CVs available online only report biographical data in narrative rather than chronological format.

previous central government work experience. Re-estimating the full model including this variable, I find that the relationship between central state-owned enterprise heads' previous government work experience and the likelihood of mergers is negative and is not statistically significant.<sup>368</sup> Table 4.6 below summarizes these results.

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<sup>368</sup> Additional research is needed to supplement the information available online in order to gather the data necessary to disaggregate the duration of central state-owned enterprise heads' previous central government experience, the specific government bodies where they worked, and the administrative rank of their positions. The negative relationship observed may be due to the broad measure of central government experienced employed here, whereby any work experience at the center of one year or more is treated as equivalent.

Table 4.6: Estimation Results for Central State-owned Enterprise Heads' Previous Work Experience at the Center

| Variable  | Model 5     |
|---|-------------|
| Industry strategic importance   | 0.730*      |
| Low   | (0.344)     |
| Industry strategic importance   | 1.338**     |
| High  | (0.316)     |
| SASAC director Li Rongrong  | 0.054       |
|   | (0.391)     |
| SASAC director Wang Yong  | -0.456      |
|   | (0.451)     |
| Central state-owned enterprise heads with previous center work experience | -0.471      |
|   | (0.354)     |
| Market competition  | -0.423      |
|   | (0.346)     |
| Size (medium)   | -1.300**    |
|   | (0.293)     |
| Size (large)  | -2.307**    |
|   | (0.569)     |
| Vice-ministerial rank   | -1.136*     |
|   | (0.549)     |
| Research institute  | -1.126      |
|   | (.580)      |
| Post-global financial crisis  | 1.208**     |
|   | (0.319)     |
| Constant  | -2.797**    |
|   | (0.519)     |
| AIC   | 0.310       |
| BIC   | -12,391.168 |
| Observations  | 1,743       |

Robust standard errors in parentheses

\*\* p<0.01, \* p<0.05

There could also be a potential interaction effect between central state-owned enterprise heads' previous work experience at the center and SASAC directors' varying emphasis on state-owned asset consolidation during their tenures. The predilection of enterprise heads with previous central government work experience to implement the policies or decisions mandated by their administrative superiors might vary depending on whether their political bosses clearly prioritize a particular course of action. The observable implication is that a central state-owned enterprise should be even more likely to experience a merger during the tenure of a SASAC director who clearly prioritizes asset consolidation (Li Rongrong) *and* when an individual with previous work experience at the center leads it. Conversely, a central state-owned enterprise should be even less likely to experience a merger during the tenure of a SASAC director who does not clearly prioritize asset consolidation (Wang Yong) *and* when an individual with previous work experience at the center leads it.

To assess possible interaction effects between central state-owned enterprise heads' previous work experience at the center and SASAC directors' varying emphasis on state-owned asset consolidation during their tenures, I re-estimate the full model including an interaction term. I find that the relationship between central state-owned enterprise heads' previous government work experience and the likelihood of mergers remains positive during the tenure of Mr. Li and negative during the tenure of Mr. Wang, consistent with the results of the previous analysis.<sup>369</sup> It is not statistically significant for either. Table 4.7 below summarizes these results.

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<sup>369</sup> While the relationship between Mr. Li's tenure and merger likelihood remains positive and that between Mr. Wang's tenure and merger likelihood remains negative, consistent with the results of the

Table 4.7: Estimation Results for Central State-owned Enterprise Heads' Previous Work Experience at the Center Interacted with SASAC Directors' Reform Strategies

| Variable  | Model 6     |
|---|-------------|
| Industry strategic importance   | 0.734*      |
| Low   | (0.344)     |
| Industry strategic importance   | 1.335**     |
| High  | (0.318)     |
| SASAC director Li Rongrong  | 0.185       |
|   | (0.431)     |
| SASAC director Wang Yong  | -0.302      |
|   | (0.491)     |
| Central state-owned enterprise heads with previous center work experience during Li Rongrong tenure | -0.842      |
|   | (0.89)      |
| Central state-owned enterprise heads with previous center work experience during Wang Yong tenure   | -1.096      |
|   | (1.342)     |
| Central state-owned enterprise heads with previous center work experience                           | 0.277       |
|   | (0.841)     |
| Market competition  | -0.429      |
|   | (0.346)     |
| Size (medium)   | -1.314**    |
|   | (0.291)     |
| Size (large)  | -2.303**    |
|   | (0.569)     |
| Vice-ministerial rank   | -1.131*     |
|   | (0.547)     |
| Research institute  | -1.129      |
|   | (0.578)     |
| Post-global financial crisis  | 1.213**     |
|   | (0.318)     |
| Constant  | -2.910**    |
|   | (0.541)     |
| AIC   | 0.309       |
| BIC   | -12,405.222 |
| Observations  | 1,743       |

Robust standard errors in parentheses

\*\* p<0.01, \* p<0.05

previous analysis, the relationship between enterprise heads' previous work experience at the center and the likelihood of merger changes from negative to positive when this interaction term is included.

Finally, one might also argue that central state-owned enterprises' economic performance is an important factor affecting their likelihood of experiencing a merger. Firms with poor economic performance may be more likely to be merged. Two key indicators of state-owned enterprises' economic performance are percentage of state-owned asset value preserved (国有资产保值增值率, *guoyou zichan baozhi zengzhi lv*) and operational income (营业收入, *yingye shouru*). Preservation of state-owned asset value refers to whether a central state-owned enterprise has succeeded in maintaining or increasing its asset value.<sup>370</sup> Losses in state-owned asset value (if the percentage of state assets preserved is less than 100%) are a salient indicator of economic performance, because although there is no publicly available information on specific levels of state-owned asset growth that a state firm must achieve, one can assume that losing asset value constitutes a red line. I therefore expect a positive relationship between losses in state-owned asset value and mergers. In addition, I expect a negative relationship between income and mergers, because SASAC may be less likely to restructure state firms that generate higher incomes due to the support they provide to the government's fiscal revenues.

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<sup>370</sup> This indicator is more appropriate than income, profits, or return on assets as an indicator of economic performance for state-owned enterprises across industries, because the government has different expectations for the performance of state-owned enterprises in different sectors. For example, SASAC assesses state-owned utilities by the stability and quality of their service provision, not their maximization of profits; indeed, price controls on electricity and oil further underscore the point that profit maximization is not these companies' primary objective. In contrast, SASAC does consider profits to assess the performance of state-owned enterprises engaged in trading or investment. For a summary of the different performance indicators for Chinese state-owned enterprises operating in public versus commercial sectors, see Central Committee of the Communist Party of China, State Council: 《国有企业改革的指导意见》 [Guiding Opinions on the Reform of State-Owned Enterprises], September 13, 2015.



I collected data on these economic performance variables but ultimately decided they could not be used due to serious concerns about bias and missing data.<sup>371</sup> I gathered data for percentage of state-owned asset value preserved and operational income for central state-owned enterprises as a whole using hundreds of pages of company-level narrative economic data and statistical tables reported in SASAC's annual yearbooks. The problem of missing data was immediately apparent: for the 1,901 firm-year observations examined here, income was reported for fewer than half; the percentage of assets preserved was reported for just one third. This raises serious concerns about data unreliability and bias due to the possibility that missing data is not missing at random, but rather reflects deliberate government withholding of data showing poor economic performance due to potential public criticism of loss of state-owned assets. Loss of state-owned assets is a sensitive issue in China because of widespread asset-stripping during state-owned enterprise reform in the 1990s and due to the Xi Jinping administration's ongoing anti-corruption campaign. Close examination of the data itself further reinforced concerns about bias: less than 5% of all firm-year observations for which data were available indicated asset loss, which seems improbably low. Moreover, I discovered that when later years of the SASAC yearbook reported performance data for earlier years, the previous years' data was systematically revised upward.<sup>372</sup> Audits conducted in 2017 by the Chinese

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<sup>371</sup> First, the possibility that missing data may not be missing at random risked introducing bias into the model estimation. Second, the scarcity of available data meant that including these variables in the main model estimation would have required dropping between one third to one half of the observations used for model estimation due to missing data.

<sup>372</sup> While adjustment of previous years' data is justifiable, the systematic trend of increase in reported performance data is a red flag.

government have revealed deliberate falsification of operational revenue, underscoring concerns about the reliability of data for this indicator as well.<sup>373</sup>

## ***Conclusion***

In this chapter, I assessed the effects of political leadership on the likelihood of mergers for all central state-owned enterprises between 2003 and 2015. Using logistic regression analysis, I evaluated three hypotheses for the incidence of mergers focused on top-level political leadership (the national leadership's official designation of industry strategic importance), middle-level political leadership (the extent to which SASAC directors' reform strategies prioritize consolidation of state-owned assets), and levels of market competition in domestic industries. I found strong support for the top-level political leadership hypothesis but little support for the middle-level political leadership and market competition hypotheses. I also found that while mergers are more likely in the period after the onset of the global financial crisis in 2008, they are less likely for larger sized firms and those with vice-ministerial rank.

Taken together, these findings suggest that a political logic crafted by top national leaders is what drove mergers among central state-owned enterprises between 2003 and 2015—not economic considerations or the political leadership of organizational leaders at lower levels. Mergers of central state-owned enterprises appear aimed at building a core group of large central state-owned enterprises concentrated in strategic sectors of the economy; they do not seem to be an

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<sup>373</sup> According to an investigation by China's National Audit Office, 18 of the 20 central state-owned enterprises audited inflated their revenue by a total of ¥200.16 billion (\$29.3 billion) in "recent years." Yu Xi, "SOEs [State-owned Enterprises] Seen Inflating Revenue," *Global Times*, June 25, 2017.

administrative method used primarily to respond to changing market conditions.<sup>374</sup>

The political design that guides mergers originates from decisions made by top national leaders regarding the strategic importance of specific industries and of particular central state-owned enterprises, the latter of which is reflected in the assignment of vice-ministerial rank to a select group of firms. Both SASAC leaders at the middle level and central state-owned enterprise heads at the company level seem to have less influence to shape economic reform that involves the restructuring of overall firms through mergers.

These findings imply three possible limits on organizational leaders' political leadership. First, organizational leaders at the central level and below may have greatest ability to shape the reform of the organizations that they lead. For example, SASAC directors may exercise more influence over the reform of SASAC itself than that of the entire portfolio of central state-owned enterprises under its administration. Second, this issue also suggests that organizational leaders' domains of authority may shrink as one moves up China's administrative hierarchy. Not only do top national leaders and their administrative superiors in the State Council limit SASAC directors' scope for autonomous influence, so too do the numerous central-level bodies that participate in various aspects of the state-owned enterprise reform process, which include but are not limited to the Central Organization Department, the National Development and Reform Commission, and now also the Central Leading Group

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<sup>374</sup> This argument is consistent with the claims of recent studies about the origins of China's large state-owned business groups and the motivations for their development. Sarah Eaton, *The Advance of the State in Contemporary China: State-Market Relations in the Reform Era* (Cambridge: Cambridge University Press, 2015); Chen Li, *China's Centralized Industrial Order: Industrial Reform and the Rise of Centrally Controlled Big Business* (New York: Routledge, 2014).

established by the Xi Jinping administration.<sup>375</sup> Third, organizational leaders' ability to exercise political leadership in the economic reform process may vary according to issue area. For example, SASAC directors may have greater autonomous influence to decide technical issues, like the specific measures used to assess state-owned enterprise performance, than they do influence major restructuring of state-owned assets through mergers. Studies of political leadership must be attentive to organization heads' jurisdictions of influence and how they vary depending on levels of administrative hierarchy and/or issue area.<sup>376</sup>

Additional data collection and alternative variable specifications could help to better isolate and assess the effects of political leadership on merger likelihood relative to other factors. For top-level political leadership, further research is essential to pinpoint the key individuals within the top national leadership and to evaluate the content and consistency of their choices and actions relevant to state-owned enterprise mergers over time. In addition, alternative variable specifications could enable more fine-grained examination of the impact of central state-owned enterprise heads' previous work experience on merger likelihood. Beyond the simple binary of having worked at the center or not, the effects of enterprise heads' work experience in central government may vary depending on its duration, the administrative rank of their positions, and the particular government bodies where they worked. It may also be that interacting central state-owned enterprise heads' previous work experience at the

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<sup>375</sup> Barry Naughton, "The Current Wave of State Enterprise Reform in China: A Preliminary Appraisal," *Asian Economic Policy Review* 12, no. 2 (2017): 282-298.

<sup>376</sup> For example, it would make little sense to study the potential impact of President Xi Jinping's political leadership on variation in the mechanisms for public participation in local budgeting that have recently emerged in some Chinese counties. Broad national policies initiated by Xi Jinping might encourage the broad goal of participatory governance, but they fall short in accounting for variation in the emergence of such governance innovations and their particular organizational forms.

center with SASAC directors' tenures does not adequately capture the dynamics of strategic interactions between enterprise heads and their administrative superiors, or the political incentives that might affect these strategic interactions. Finally, further data collection on the economic performance of central state-owned enterprises' publicly listed subsidiaries offers another possible way to make baseline estimates about their overall economic performance. While this approach would also confront the challenge of missing data, it would enable the analysis to take enterprise performance into account without employing problematic data from SASAC yearbooks.

In conclusion, this study suggests multiple areas for future research. First, while this chapter analyzes variation in the incidence of mergers among central state-owned enterprises, it does not disaggregate variation in the types of mergers themselves. If these mergers indeed reflect an underlying political logic, then more fine-grained study of different types of mergers might illuminate some of its key features. For example, such analysis could differentiate between mergers between small and large firms versus those involving two large firms, or mergers that link firms in upstream and downstream industries versus those that involve horizontal industry tie-ups. In addition, despite the previous chapter's contention that domestic reform and globalization are increasingly intertwined, an important limitation of this study's analysis is its lack of variables that capture the relative extent of central state-owned enterprises' activity in international markets. This is due not only to the lack of publicly available data on central state-owned enterprises' commercial activities overseas, but also because of the difficulty of identifying internationally-oriented

variables that would be meaningful for central state-owned enterprises across industries.<sup>377</sup> Given the growing importance of Chinese state-owned enterprises in international markets, this is an important area for future data collection and analysis. Finally, additional research is needed to assess whether this study's findings can be extended beyond the population studied here—Chinese central state-owned enterprises between 2003 and 2015. For example, future studies could analyze the factors that affect the likelihood of mergers among the large body of state-owned enterprises owned by governments below the central level.

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<sup>377</sup> For example, the RMB exchange rate may strongly affect those central state-owned enterprises heavily involved in exports, trade or investment, but have much less impact on others. Similarly, levels of exports or overseas mergers and acquisitions cannot be used to measure the internationalization of central state-owned enterprises across industries, because some of the state firms under SASAC's management (for example, research and design institutes) exhibit little activity in these areas.

## Chapter 5

### **Co-evolutionary Analysis of Economic Reform:**

#### **Linking Political Leadership with Organizational and Institutional Change**

The institution of state ownership in China has transformed dramatically in its scope, function, and orientation since the initiation of market-oriented reforms in 1978.<sup>378</sup>

Whereas state ownership was synonymous with the state's ownership and control of assets at the start of the reform era, its scope has now broadened to encompass the ownership and control of capital as well as assets. The state has also gradually permitted non-state shareholders, including private sector actors, to exercise limited ownership and control rights over state-owned assets and capital. State ownership in the national economy has declined overall but has also become increasingly concentrated in a select group of large industrial conglomerates in sectors deemed critical to national development and security. Instead of ascribing strategic importance to state ownership as a whole, the government now differentiates among state-owned enterprises' strategic importance based on industry and firm type.<sup>379</sup> Finally, state

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<sup>378</sup> I define state ownership as rights of ownership and control over assets and/or equity that are vested in the state as opposed to a private sector actor or individual; it is distinct from public ownership because these rights are restricted and a government body exercises them.

<sup>379</sup> The Chinese government first officially differentiated the strategic importance assigned to state ownership in 1999 by specifying that state ownership should maintain the "dominant position" (支配地位, *zhipei diwei*) in "important industries and key areas" (重要行业和关键领域, *zhongyao hangye he guanjian lingyu*)—as well as "backbone enterprises in important industries" (重要产业中的骨干企业, *zhongyao chanye zhong de guban qiye*). It named three important industries and one key area. In 2006, the State Council further differentiated the strategic importance assigned to state ownership by enumerating seven industries where the state will keep "absolute control" and nine industries where it will maintain "strong influence." Central Committee of the Communist Party of China: 《中共中央关于国有企业改革和发展若干重大问题的决定》 [The Decision of the Central Committee of the Communist Party of China on Major Issues Concerning the Reform and Development of State-Owned Enterprises], September 22, 1999. 《我国明确七大行业将由国有经济保持绝对控制力》 [China

ownership's original orientation toward an internationalizing domestic market has expanded to include state-owned enterprises' engagement in world markets and their ownership and control of both assets and capital overseas. What factors explain these far-reaching changes in the institution of state ownership in China?

One explanation of change in state ownership in China focuses on the intertwining of political competition among top national leaders and intellectual debate among government-affiliated economists. Indeed, the shifting influence at the center of individuals like Deng Xiaoping, Zhao Ziyang, Jiang Zemin and others did profoundly shape the institution of state ownership. Through their final authority over reform policy-making and the initiation and design of pilot programs, they exerted important influence on the content, timing, and sequencing of changes in state ownership. Also critical were the ideas, writings, and domestic and international exchanges carried out by economists like Xue Muqiao, Sun Yefang, Liu Guoguang, Dong Furen, Wu Jinglian, Zhao Renwei, Gao Shangquan, Zhou Xiaochuan, Lou Jiwei, and myriad others.<sup>380</sup> Their intellectual output was a vital input in debates among top national leaders and ongoing processes of reform policy-making and experimentation; some even went into government themselves.<sup>381</sup> Top national leaders and economists at the center thus remain the primary institutional architects of state ownership according to this explanation.

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Specifies Seven Major Industries Where the State-owned Economy Will Maintain Absolute Control], 《上海证券报》 [Shanghai Securities News], December 19, 2006.

<sup>380</sup> Shitao Fan and Isabella Weber, "From Control of the 'Commanding Heights' to Control of the Whole Economy and Back: Chinese Ownership Theories Since 1949" (forthcoming); Joseph Fewsmith, *Dilemmas of Reform in China: Political Conflict and Economic Debate* (Armonk, NY: M.E. Sharpe, 1994); Julian Gewirtz, *Unlikely Partners: Chinese Reformers, Western Economists, and the Making of Global China* (Cambridge, MA: Harvard University Press, 2017).

<sup>381</sup> Examples include Xue Muqiao, Liu Guoguang, and Wu Jinglian.



Another explanation extends the premise of “state-led” change downward to argue that local governments generate change in state ownership.<sup>382</sup> It inverts focus on the center as a unitary “owner” in the institution of “state ownership” by suggesting that “there potentially are as many owners...as there are government jurisdictions.”<sup>383</sup> While local governments do not operate autonomously of the center, they do drive evolution in state ownership by determining the form and pace of institutional change in particular localities. Property rights at the local level are thus ultimately constructed through processes of interpretation and negotiation that local governments lead.<sup>384</sup> Institutions designed at the center constrain and incentivize local governments; at the same time, local governments can act as “institutional entrepreneurs” by creatively remaking or repurposing existing institutions.<sup>385</sup> Local governments may also close the “institutional gaps” necessary for institutional transformation in state ownership to occur, through ad-hoc practices that enabled privatization to proceed and maintained social stability despite rising unemployment.<sup>386</sup> In summary, this explanation suggests that local governments—individually and in their interactions with the center—drive institutional change.

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<sup>382</sup> Jin Zeng, *State-led Privatization in China: The Politics of Economic Reform* (Milton Park, NY: Routledge, 2013).

<sup>383</sup> Andrew G. Walder, “Local Governments as Industrial Firms: An Organizational Analysis of China's Transitional Economy,” *American Journal of Sociology* 101, no. 2 (1995): 270.

<sup>384</sup> Meg E. Rithmire, *Land Bargains and Chinese Capitalism: The Politics of Property Rights under Reform* (New York: Cambridge University Press, 2015); Adam Segal, *Digital Dragon: High-technology Enterprises in China* (Ithaca, NY: Cornell University Press, 2003).

<sup>385</sup> Institutional entrepreneurship refers to “activities of actors who have an interest in particular institutional arrangements and who leverage resources to create new institutions or to transform existing ones.” Steve Maguire, Cynthia Hardy, and Thomas B. Lawrence, “Institutional Entrepreneurship in Emerging Fields: HIV/AIDS Treatment Advocacy in Canada,” *Academy of Management Journal* 47, no. 5 (2004): 657.

<sup>386</sup> Jin Zeng and Kellee S. Tsai, “The Local Politics of Restructuring State-owned Enterprises,” *Going Private in China: The Politics of Corporate Restructuring and System Reform*, ed., Jean C. Oi, (Walter H. Shorenstein Asia-Pacific Research Center Books, 2011).

However, these two explanations of change in state ownership lack a dynamic organizational dimension. They do not specify the nature of the relationship between institutions and organizations—or even distinguish conceptually between them. Instead, they frequently portray institutions as somehow separate from organizational politics and change: something designed by political elites at the center or refashioned by local governments. But institutional change is inseparable from organizational change, because the institution of state ownership is embodied in organizations—from state-owned companies to development banks to sovereign wealth funds to government ownership agencies. Instead of recognizing political leadership as a driver of organizational change, these explanations instead attribute variation in organizational structures and strategies to resource endowments, institutional legacies and incentives, or the external environment. Finally, these explanations fail to fully take into account the feedback loops—flows of information and personnel—that link not only the center with localities but also organizations at the same level with one another. In addition to experimental pilot schemes and the promotion and rotation of officials, multiple other forms of formal and informal exchanges function to reinforce or to generate change in existing institutions.

In this chapter, I introduce a co-evolutionary approach to analyzing economic reform that links the micro-level organizational change wrought by political leadership with macro-level institutional change. Three specific aspects of co-evolution inspire this approach. First, co-evolution's emphasis on mutual interdependence—and ultimately mutual constitution—suggests that institutions change because of changes in the behavior and structure of the organizations that constitute them. This diverges

from accounts that attribute institutional change to exogenous factors—such as economic shocks or regime change—or to endogenous change occurring within a single entity and not multiple mutually interdependent ones. Second, its emphasis on dynamic linkages—flows of information and personnel—draws attention to the multi-directionality of influence among actors and the feedback loops that link organizations with organizations and organizations with institutions. Rather than viewing institutions solely as top-down constraints on organizational and individual behavior, a co-evolutionary approach shows that changes at—and crucially, originating from—the organization level can directly influence the maintenance, modification, or demise of existing institutions. Third, a co-evolutionary approach to analyzing economic reform underscores processes of experimentation, competition, and selection.<sup>387</sup> While organizational leaders are the primary agents of experimentation and competition, the state influences these processes and ultimately selects winners and losers.

Political leadership at the organization level is central to co-evolutionary analysis of economic reform. Co-evolution does not occur spontaneously or without direction. Instead, organizations and institutions co-evolve as organizational leaders make choices about whether and how to alter given organizational structures and strategies. Through political leadership, heads of organizations mediate how institutional incentives and pressures influence their organizations and how their organizations respond to changes in the behavior of others. Political leadership also

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<sup>387</sup> In this chapter I focus on experimentation, which includes actors' reactive changes in response to external factors (such as other organizations and their institutional environment) as well as their proactive behavior to change that external environment. While I engage research on adaptation, I do not use this concept because it privileges the influence of external factors on actors' behavior. Emphasizing the reactive nature of behavior by organizations and their leaders obscures the ways in which they may not only respond to—but also proactively seek to shape—other organizations and their institutional environments.

helps to explain the wide variation possible among the structures and strategies of similar organizations in a common institutional environment, or within a single organization over time. The organizational change shaped by political leadership at the micro-level can generate co-evolution in the particular institutions that organizations embody and potentially even the broader institutional environment.<sup>388</sup>

### ***A Co-evolutionary Approach to Analyzing Economic Reform***

Co-evolutionary analysis draws inspiration from the shared insight of systems theory, complexity research, and economic sociology that dynamic interactions among actors can generate institutional change. Systems theory emphasizes the importance of studying biological and social systems as integrated wholes; it suggests that their properties emerge from interactions among the elements of interpenetrating systems.<sup>389</sup> These systems are characterized by their degrees of complexity (the non-linear nature of the relationships among their elements, which means that multiple solutions can emerge from the same set of inputs); openness (the flows of information, energy, and matter linking them with external environments); and capacity for adaptation (the ability of their elements to respond to these environments). Although biological and social systems alike evolve in open-ended and unpredictable ways, they can be stable over long periods of time and exhibit self-regulation.<sup>390</sup> From a systems

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<sup>388</sup> An institutional environment refers to a negotiated, emergent, and dynamic constellation of multiple institutions. Definition adapted from Lynne G. Zucker, "Institutional Theories of Organization," *Annual Review of Sociology* 13, no. 1 (1987): 447.

<sup>389</sup> Systems are differentiated through the "self-referential" nature of their operations; at the same time, they remain open to and dependent on their external environment, which may also include other systems. Niklas Luhmann, *Social Systems* (Palo Alto, CA: Stanford University Press, 1995): 37-41.

<sup>390</sup> Von Bertalanffy 1952 identifies the characteristic properties of systems as "mutual interdependence, self-regulation, adaption to disturbances, approach to states of equilibrium...." Ludwig von Bertalanffy,

theory perspective, institutions emerge from and change with the patterns of social relations that occur within interpenetrating systems.

However, while systems theory usefully underscores the complexity and fundamental unpredictability of economic and political systems, it leaves little space for actor-based analysis of institutional change. A strict interpretation of systems theory implies that it is both practically and theoretically impossible to isolate the roles of discrete actors (such as local governments, enterprises, organizations, or individuals) in processes of institutional change. Even applied more loosely, system theory's operational orientation at the system level makes it poorly suited for analyzing the sub-system hierarchies of influence among actors that shape system-level processes such as selection and the emergence and operation of feedback loops. System theory's emphasis on system-wide dynamics like competition also overlooks a range of actor-centered political behavior rooted in these hierarchies of influence, from accommodation to negotiation to domination.

Complexity research focuses greater attention on the actors in a particular system and their interactions, strategies, and learning. It suggests that institutions emerge from patterns of interaction among actors in a system and that they change through ongoing, open-ended processes of mutual adaptation shaped by that system's selection criteria.<sup>391</sup> Unlike systems theory, complexity research does acknowledge the possibility that particular actors, such as central authorities, may exert dominant

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*Problems of Life: An Evaluation of Modern Biological and Scientific Thought* (New York: Harper, 1952): 51-53.

<sup>391</sup> Ang 2016 and Axelrod and Cohen 1999 point out that how success is defined in the selection environment of social systems may vary widely, unlike in biological systems where survival and reproduction constitute "success." Yuen Yuen Ang, *How China Escaped the Poverty Trap* (Ithaca, NY: Cornell University Press, 2016); Robert M. Axelrod and Michael D. Cohen, *Harnessing Complexity: Organizational Implications of a Scientific Frontier* (New York: Free Press, 1999).

influence over others.<sup>392</sup> Yet its baseline for analysis remains the emergent attributes of the system as a whole and its main focus the effectiveness of particular interventions, rather than influential actors' attributes, motivations, or actual behavior. Axelrod and Cohen (1999) describe the aims of complexity theory in the context of hierarchies of political influence as "to understand how those dominant influences come about, what sustains (or undermines) them, and how local action responds in the face of global constraints."<sup>393</sup> Yet this overlooks what influential actors actually do with the relative autonomy they enjoy—political leadership—and its effects beyond potentially inducing mimicry.<sup>394</sup> More broadly, complexity research's emphasis on the dynamics of adaptation ultimately restricts both the possible scope of individual action and its consequences. Focusing on adaptation and innovation, both of which involve responding to existing—even if newly emergent—ways of doing things, forecloses the possibility of genuine novelty, however rare, through truly open-ended processes of experimentation and invention.<sup>395</sup>

Economic sociology shifts the locus of institutional change from systems to discrete, inter-connected networks among organizations and individuals. Seminal

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<sup>392</sup> For example, central authorities or other influential actors may carry out social interventions aimed deliberately at altering the interactions among actors within and across particular systems, such as: segregation and integration policies, zoning restrictions, immigration rules, and sub-national and international educational exchanges or training programs. Axelrod and Cohen (1999): 21.

<sup>393</sup> Ibid: 18.

<sup>394</sup> Axelrod and Cohen 1999 state that actors are likely to copy the visible behavior of leaders, especially in periods of uncertainty and rapid change, because leaders set standards, establish norms, and their behavior is assumed to embody criteria of success. However, inducing mimicry by peers and subordinates is just one possible effect of political leadership. Moreover, in some selection environments, differentiation through niche creation—not only mimicry—is ultimately the best strategy for success. Ibid: 148-150.

<sup>395</sup> Powell and Padgett 2012 contrast innovation, activities that generate improvements on existing ways of doing things, with invention, activities that fundamentally change existing ways of doing things. John F. Padgett and Walter W. Powell, "The Problem of Emergence," John F. Padgett and Walter W. Powell, eds., *The Emergence of Organizations and Markets* (Princeton, NJ: Princeton University Press, 2012).

work on social embeddedness and its argument that economic transactions occur through social relationships does assume some degree of autonomy at the individual level.<sup>396</sup> However, networks, not the individual actors they comprise, are the primary agents of institutional change in economic sociology.<sup>397</sup> Economic sociology offers important insights into sub-institutional dynamics, such as how networks operate to create and regulate norms and to solve problems of trust.<sup>398</sup> However, it too pays less attention to how intra-organizational politics and hierarchies of influence among individuals and among and within organizations shape organizational and institutional change. Norms do not constrain all individuals equally; those in positions of influence have greater scope for action.<sup>399</sup> Moreover, heads of organizations can change organizational structure or mediate among competing actors within a network, thereby shaping new patterns of organizational and individual behavior, and ultimately generating institutional change.

Co-evolutionary analysis builds on systems theory, complexity research, and economic sociology approaches to studying institutional change. It embraces their

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<sup>396</sup> Mark Granovetter, "Economic Action and Social Structure: The Problem of Embeddedness," *American Journal of Sociology*, 91, no. 3 (1985): 481-510.

<sup>397</sup> On networks in economic sociology, see Victor Nee, "The New Institutionalisms in Economics and Sociology," *The Handbook of Economic Sociology*, eds. Neil Smelser and Richard Swedberg (Princeton, NJ: Princeton University Press, 2005).

<sup>398</sup> These studies examine the structure of networks and its effects. Pierre Bourdieu, "The Forms of Capital," *Handbook of Theory and Research for the Sociology of Education*, ed. John Richardson (New York: Greenwood, 1986): 241-258; James S. Coleman, "Social Capital in the Creation of Human Capital," *American Journal of Sociology* 94 (1988): 95-120; Alejandro Portes and Julia Sensenbrenner, "Embeddedness and Immigration: Notes on the Social Determinants of Economic Action," *The American Journal of Sociology*, 98, no. 6 (1993): 1,320-1,350.

<sup>399</sup> The concept of brokerage by actors with bridging ties across "structural holes" and/or exclusive ties engages the possibility for particular actors to exercise disproportionate influence or even to change market structure; however these studies focus primarily on questions of information flows, transaction costs, and organizational structure, not intra-organizational politics. Ronald S. Burt, *Structural Holes: The Social Structure of Competition* (Cambridge, MA: Harvard University Press, 2009); Neil Fligstein, *The Architecture of Markets: An Economic Sociology of Twenty-First-Century Capitalist Societies* (Princeton, NJ: Princeton University Press, 2002).

process orientation and the idea that institutions are inseparable from the activities of actors at all levels. However, it takes organizations and even individual actors—not systems or networks—as the key units of analysis in institutional continuity and change. Three specific aspects of co-evolution provide the building blocks for a co-evolutionary approach to analyzing economic reform. First, co-evolution underscores the mutual interdependence—and ultimately mutual constitution—of institutions and organizations. Not only can change in institutions during economic reform impact how organizations are structured and behave, change in organizational structure and behavior can also generate corresponding change in institutions. Second, co-evolution underscores the dynamic linkages—flows of information and personnel—among actors that can generate change in organizations and institutions alike. These dynamic linkages provide the potential for multi-directional influence and can also generate feedback loops that function to reinforce or alter existing institutions. Third, co-evolution highlights both the dynamics of experimentation, competition, and selection, as well as the hierarchies of political influence that are central to interlinked processes of organizational and institutional change. In the following sections, I discuss these three elements of co-evolutionary analysis and then explain how political leadership is integral to each.

The first element in a co-evolutionary approach to analyzing economic reform is the mutual interdependence of institutions and organizations. In the context of economic reform, this suggests that we should think of institutions such as state ownership as embodied in and shaping the behavior of organizations—like state-owned enterprises and government ownership agencies—but also as simultaneously



being affected by changes in the structure and behavior of these organizations.

Institutions function to constrain and guide both individual and organizational actors' behavior in important ways: by shaping their relationships, defining their positions in those relationships, and guiding interaction among them by providing shared sets of meanings as the basis for their own behavior and for interpreting the behavior of others.<sup>400</sup> Institutional environments can also constrain the repertoire of possible organizational forms through processes of coercion, mimicry, and normative pressure.<sup>401</sup> But institutions do not determine organizational actors' behavior, and they are also subject to influence by it.<sup>402</sup> As Paul Ingram (1998) writes: "Since institutions determine the opportunities and incentives that determine outcomes for actors, and because institutions are humanly devised, we should expect actors to try to influence institutions."<sup>403</sup> In some cases, this process of influence occurs through deliberate negotiation among multiple actors.<sup>404</sup> In other cases, it takes the form of uncoordinated

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<sup>400</sup> Neil Fligstein, "Social Skill and Institutional Theory," *American Behavioral Scientist* 40, (1997): 397-405.

<sup>401</sup> Constraint on organizational repertoires can arise through these institutional channels and through competition, as organizations with non-optimal forms and behaviors are eliminated. Paul DiMaggio and Walter W. Powell, "The Iron Cage Revisited: Collective Rationality and Institutional Isomorphism in Organizational Fields," *American Sociological Review* 48, no. 2 (1983): 147-160.

<sup>402</sup> Even Hannan and Freeman 1977, who focus primarily on the process of selection by which organizations with non-optimal forms and behaviors are eliminated, acknowledge that organizational decision-makers' response to their external environments—not only the conditions of those environments themselves—can determine survival. Michael T. Hannan and John Freeman, "The Population Ecology of Organizations," *American Journal of Sociology* 82, no. 5 (1977): 930.

<sup>403</sup> Ingram 1998 shows how hotel organizations in the United States—in particular a coalition of presidents of large hotel chains—changed institutions related to training and education in the hospitality industry. He concludes: "Ultimately, institutional dynamics cannot be separated from organizational dynamics." Paul Ingram, "Changing the Rules: Interests, Organizations, and Institutional Change in the U.S. Hospitality Industry," *Institutionalism in Sociology*, eds., Mary Brinton and Victor Nee (Russell Sage Foundation, 1998): 258, 273-274.

<sup>404</sup> For instance, Rithmire 2015 argues that political bargaining between local governments and state bodies and social groups generates variation in property rights institutions at the local level in China. Rithmire 2015: 20.

strategic behavior by a group of actors.<sup>405</sup> In still other cases, actors may unintentionally create institutional variation and change.<sup>406</sup> No matter whether actors set out to modify existing institutions or trigger a series of unintended effects through their behavior, they can still generate what Colin Hay and Daniel Wincott (1998) term “direct effects”: “a partial transformation of that institutional environment (though not necessarily as anticipated) and altering the course of its temporal unfolding (however marginally).”<sup>407</sup>

Second, a co-evolutionary approach to analyzing economic reform underscores the dynamic linkages that connect actors and generate organizational and institutional continuity as well as change. These dynamic linkages consist of information and personnel flows among individuals and organizations. As individuals move from one organization to another, they bring a particular set of knowledge, skills, and relational protocols into the new environments in which they are “transposed.”<sup>408</sup> At the same

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<sup>405</sup> For example, Nee and Oppor 2012 describe how private entrepreneurs in China during the 1990s exploited the creation of new legal categories for corporate organization, such as state-owned business groups, limited liability corporations, and joint stock companies. Private entrepreneurs strategically registered their companies as limited liability corporations to gain the legitimacy necessary to survive in China’s fledgling markets, since this organizational form also included state-owned enterprises. In doing so, they aided the emergence of capitalist market institutions and a private enterprise economy. See Chapter 5, “Legitimacy and Organizational Change,” Victor Nee and Sonja Oppor, *Capitalism from Below: Markets and Institutional Change in China* (Cambridge, MA: Harvard University Press, 2012). See also David Daokui Li, Junxin Feng, and Hongping Jiang, “Institutional Entrepreneurs,” *The American Economic Review* 96, no. 2 (2006): 358-362.

<sup>406</sup> For example, Saxenian 1994 describes how former Stanford University president Frederick Terman’s view of the university as a “community of technical scholars” prompted him to establish the Stanford Research Institute, Stanford Industrial Park, and the Honors Cooperative Program. This created new linkages between academia and industry and ultimately contributed to the development of a distinct regional economy in California’s Silicon Valley. Annalee Saxenian, *Regional Advantage: Culture and Competition in Silicon Valley and Route 128* (Cambridge, MA: Harvard University Press, 1994).

<sup>407</sup> Colin Hay and Daniel Wincott, “Structure, Agency and Historical Institutionalism,” *Political Studies* 46 (1998): 956.

<sup>408</sup> For further discussion of the concept of transposition and its consequences specifically for changes in organizational structure, see John F. Padgett, “Transposition and Refunctionality: The Birth of

time, heads of organizations constantly make choices about whether to maintain or alter existing organizational strategies and structures in response to the behavior and structure of other organizations and to the institutional environments in which they operate. Dynamic linkages connecting actors with one another and their institutional environments matter because they create the potential for multi-directional influence. Each actor has the capacity to influence others and its institutional environment, although in practice capacity for influence varies widely. Finally, these dynamic linkages can give rise to feedback loops.<sup>409</sup> While these feedback loops can sustain and enforce existing institutions, they can also spread alternative ideas and practices with the potential for ultimately transformative effects.<sup>410</sup>

Third, a co-evolutionary approach to analyzing economic reform highlights processes of experimentation, competition, and selection. The central state as well as organizations and their leaders participate in each of these processes. The center may seek to influence the aims and scope of experimentation, for example by delineating its goals, carrying out pilot programs, and selecting model organizations and disseminating successful experiences. At the same time, heads of organizations formulate and choose among multiple possible ways to alter organizational strategies and structures in response to central reform goals. They may also engage in

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Partnership Systems in Renaissance Florence,” *The Emergence of Organizations and Markets*, eds., John F. Padgett and Walter W. Powell (Princeton, NJ: Princeton University Press, 2012).

<sup>409</sup> A feedback loop is a pathway by which some of the output of a particular situation becomes new input, generating a cyclical flow that ultimately produces either more or less of the same effect.

<sup>410</sup> As Saxenian and Lee 2007 write: “... When it comes to a set of rules, standards, norms and conventions that are to be reproduced and improvised by daily practices, then, through the orchestration of strategic purposes and deliberate actions, microevents and occurrences may lead to structural changes that start off a new path of development.” Chuan-Kai Lee and Annalee Saxenian, “Coevolution and Coordination: A Systemic Analysis of the Taiwanese Information Technology Industry,” *Journal of Economic Geography*, 8, no. 2 (2007): 159.

experimentation outside the bounds of the center's directives, especially in situations of high ambiguity or uncertainty about the goals of reform and its methods. In addition, co-evolutionary analysis of economic reform underscores how competition among actors occurs in multiple selection environments—both economic and political. Individuals compete for political promotion not only by steering their organizations to perform well relative to others, but also through differentiating themselves from their peers and predecessors. The center mediates this competition among actors; however, it is not an impartial referee that defines the criteria of success for this competition and then steps back until winners appear. Certain organizations and their heads may gain disproportionate political and material support based on their personal connections or if their approaches accord with the preferred policy agenda of particular political elites.<sup>411</sup> Finally, the center selects the winners and losers of competition and rewards individuals and organizations with political and/or material benefits.

Political leadership is integral to all three elements of co-evolutionary analysis. First, it lies at the heart of the mutual interdependence of institutions and organizations. Institutions exert important influence on organizations and their heads, but they do not control them. Organizational leaders still possess bounded autonomy to exercise political leadership through choosing whether and how to maintain or to modify existing organizational strategies and structures. The organizational change fashioned by their political leadership can in turn generate corresponding change in the institutions that their organizations constitute. Individual and organizational actors

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<sup>411</sup> Hongbin Cai and Daniel Treisman, "Did Government Decentralization Cause China's Economic Miracle?" *World Politics* 58, no. 4 (2006): 505-535.

may generate institutional change either unintentionally or deliberately through individual or collective efforts to alter institutions to their benefit.

Political leadership is also crucial in the dynamic linkages—flows of information and personnel—that provide the potential for multi-directional influence and generate feedback loops that reinforce or alter existing institutions. Heads of organizations make choices about the content, amount, and veracity of the information that they share with peers and superiors through both formal and informal channels. They also decide whether and how to respond to and use the information they receive. If the center disseminates information about a model enterprise, for instance, other enterprise heads must assess its appropriateness and lessons for their own organization, weigh the costs and benefits of altering their own organizational strategies and structure in line with the model (either superficially or substantively), decide whether to do so or not, and finally determine how to act based on that decision.

Finally, political leadership is fundamental to processes of experimentation, competition, and selection. Experimentation itself is in significant part the exercise of political leadership, as heads of organizations formulate and choose among multiple possible ways to alter organizational strategies and structures in response to central reform goals and lead their subordinates to carry them out. Furthermore, political leadership is not only a method of seeking to deliver performance gains, it is also a means by which heads of organizations attempt to differentiate themselves from both their peers and predecessors in order to stand out for political promotion. The state's selection of winners and losers—organizations and individuals alike—thus turns not

only on organizational outcomes (performance) and personal ties (connectedness) but also on how well organization heads succeed in political product differentiation.

### ***Political Leadership: The Missing Factor***

A growing body of research in political economy employs the concept of co-evolution to analyze interlinked processes of organizational and institutional change.<sup>412</sup> From dye companies and national institutions in Germany, to national champions and developmental states in East Asia, to local governments and market institutions in China, this diverse literature advances a common argument that change in organizations and institutions is deeply intertwined. But what drives and mediates their co-evolution? Co-evolution of institutions and organizations does not occur spontaneously or without direction. I argue that political leadership at the organization level is an important factor driving and mediating this process. This section of the chapter first reviews three key works applying the concept of co-evolution to study organizational and institutional change. It then analyzes each of these works to show how political leadership is integral to the co-evolutionary processes they posit.

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<sup>412</sup> Early studies examining the co-evolution of institutions and organizations include Clemens 1993 and Haveman and Rao 1997. Clemens 1993 shows how women in the United States during the Progressive Era altered the structures and strategies of the existing organizational form of women's groups to imbue them with new political purpose. This organizational change was both impacted by and in turn drove an institutional shift in American democracy in which party voting declined and interest group politics became more prominent. Haveman and Rao 1997 show how institutional definitions, rules, and expectations changed in tandem with organizational structures and processes in the thrift industry during the same era. Elisabeth S. Clemens, "Organizational Repertoires and Institutional Change: Women's Groups and the Transformation of U.S. Politics, 1890-1920," *American Journal of Sociology* (1993): 755-798; Heather A. Haveman and Hayagreeva Rao, "Structuring a Theory of Moral Sentiments: Institutional and Organizational Coevolution in the Early Thrift Industry," *American Journal of Sociology* 102 (1997): 1,606-1,651.

In an influential early study, Johann Peter Murmann (2003) argues that German dye companies actively shaped national institutions in Germany during the nineteenth and twentieth centuries, just as national institutions shaped these firms' development.<sup>413</sup> Murmann analyzes two processes of co-evolution: between German industry and the university system, and between German dye firms and domestic law. Latecomers to global chemicals markets, German firms confronted shortages of trained personnel, limited resources for scientific research and development, and limited legal protections for their technological innovations. However, personnel exchanges and the formation of commercial ties drew German universities and dye firms closer, ultimately yielding a coalition of industrialists, academics, and government officials. This coalition reshaped national educational institutions by lobbying successfully for greater policy and financial support for research and training relevant to the dye industry.<sup>414</sup> In addition, German dye firms advocated for changes in German patent laws that would favor domestic firms, thereby giving them a competitive advantage in the protection of new technologies and incentivizing further technological development. By deliberately altering their selection environment, German dye firms catalyzed a positive feedback loop that ultimately enabled them to become global industry leaders.

Henry Wai-chung Yeung (2016) presents a novel analysis of industrial transformation and the developmental state in East Asia with both evolutionary and

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<sup>413</sup> Johann Peter Murmann, *Knowledge and Competitive Advantage: The Coevolution of Firms, Technology, and National Institutions* (New York: Cambridge University Press, 2003). See especially Chapter 4, "The Co-evolution of National Industries and Institutions."

<sup>414</sup> Murmann 2003: 211-213.

co-evolutionary elements.<sup>415</sup> Yeung concurs that developmental states in South Korea, Singapore, and Taiwan played crucial “midwifery” and “husbandry” functions by first establishing and supporting strategic industries and national champions during the early stages of their development.<sup>416</sup> As these national firms expanded into international markets, they became increasingly embedded in global production networks and began to engage in “strategic coupling” with leading global firms. Yeung argues that these partnerships with extra-national actors have transformed national firms, thereby also prompting the co-evolution of East Asian states. In these “post-developmental states,” the state’s developmental functions are less important and today’s national champions—made stronger and less reliant on the state through “strategic coupling”—are part of a far more diverse group of capitalist firms.<sup>417</sup>

Yuen Yuen Ang (2016) focuses on reform-era China to argue that economic development is a co-evolutionary process in which states and markets mutually adapt.<sup>418</sup> States and markets co-evolve in an incremental, iterative process as bureaucratic agents, especially at the local level, use existing weak institutions to build markets that then reinforce those institutions.<sup>419</sup> Ang describes how the center fosters an adaptive, bottom-up search for solutions through “directed improvisation.” In this process, the center aims to influence, but not control, local officials by: setting broad reform goals that authorize yet guide policy localization; defining and rewarding

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<sup>415</sup> Henry Wai-chung Yeung, *Strategic Coupling: East Asian Industrial Transformation in the New Global Economy* (Ithaca, NY: Cornell University Press, 2016).

<sup>416</sup> Peter B. Evans, *Embedded Autonomy: States and Industrial Transformation* (Princeton, NJ: Princeton University Press, 1995).

<sup>417</sup> Yeung 2016: 40.

<sup>418</sup> Yuen Yuen Ang, *How China Escaped the Poverty Trap* (Ithaca, NY: Cornell University Press, 2016).

<sup>419</sup> Ang divides bureaucratic agents into two groups: “elite bureaucrats” (the approximately 500,000 officials with county-level administrative rank and above) and “regular bureaucrats” (a grouping she estimates in the tens of millions). Her account focuses on the former. Ang 2016: 65-66.



bureaucratic success through the Chinese Communist Party's cadre management system; and encouraging officials to engage in exchanges with other localities. In response, local officials drive experimentation and generate variation by determining specifically how to implement (or not to implement) the center's policy directives in particular localities and at particular points in time.

Political leadership at the organization level plays a key but underappreciated role in the co-evolutionary processes in every one of these works. While Murmann discusses organizational leaders in industry and government, he fails to highlight the critical role of their political leadership. Yet a closer read suggests that the co-evolutionary development of German dye companies and national institutions would have been impossible without it. For example, one might argue that Friedrich Althoff, a top government official in the education ministry in Prussia, created the conditions for this co-evolution by prioritizing scientific research and training in German academia and curtailing universities' autonomy to appoint faculty.<sup>420</sup> These actions doubly amplified the dye industry's political influence. The political leadership of Henry Bottinger, head of leading German dye firm Bayer Cooperation, was also critical in this co-evolutionary process. Mr. Bottinger was instrumental in gaining state support for the dye industry by mobilizing collective associations like the German Chemical Industry Corporation and through his own direct lobbying of government officials as a member of Parliament.<sup>421</sup> These examples suggest that political leadership was indispensable in creating the flows of information and personnel that

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<sup>420</sup> Murmann 2003: 167.

<sup>421</sup> Murmann 2003: 169-170, 172.

resulted in mutual influence and change; feedback loops between national institutions and dye firms would not have arisen on their own.

Political leadership also plays a central role in Yeung's analysis of "strategic coupling" between East Asian national champions and leading global multinationals. In Yeung's account, "transnational technopreneurs" establish and mediate the networks through which national champions partner with global multinationals and transform themselves in the process, prompting simultaneous co-evolution between national champions and developmental states. But these transnational technopreneurs are more than just interchangeable "relational bridges" that catalyze and facilitate novel network ties among firms.<sup>422</sup> First, transnational technopreneurs must decide whether to prioritize strategic couplings, and if so, then which to engage in. Take for example the case study of Venture Manufacturing Singapore, led by Ngit Liong Wong as chairman and chief executive officer since 1986. Yeung describes how no one client accounted for more than 10% of Venture's revenue in 1993, but by 2005 more than 80% of its revenue came from 12 clients, including Hewlett Packard with a share of 25%.<sup>423</sup> Not only did Mr. Wong's strategy for Venture's development prioritize the establishment of strategic partnerships, as Yeung describes: "Venture has been careful and selective in partnering with specific global lead firms."<sup>424</sup> In addition, transnational technopreneurs make choices about how to alter the structures of their organizations throughout the course of the couplings. For example, Yueng describes how Mr. Wong led Venture to improve its design, manufacturing and service delivery

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<sup>422</sup> Yeung 2016: 107.

<sup>423</sup> Ibid: 107-108.

<sup>424</sup> Ibid 2016: 108.

capacities through new technology alliances with suppliers and other high-tech firms in order to fulfill the specific needs of its strategic partner firms like Hewlett-Packard.<sup>425</sup> In short, organization heads determine how to respond to and to utilize the new resources and opportunities (such as technology and markets) that both developmental states and these strategic couplings create.

Finally, Ang's argument about the co-evolution of markets and institutions in reform era China is persuasive but incomplete without consideration of political leadership. Take for example the case study of "Forest Hill," a city in Fujian province.<sup>426</sup> After improving regional transportation links through a flurry of infrastructure construction in the late 1990s, "Forest Hill" proceeded to aggressively court capital and investments through personal networks in order to grow the economy, and then finally pursued improvements in the quality of growth by fostering economic specialization and technological upgrading. Ang distills the developmental trajectory of "Forest Hill" to illustrate her thesis on the co-evolution of institutions and markets: weak institutions are harnessed to build markets, emerging markets stimulate strong institutions, and strong institutions preserve markets.

However, a political leadership argument, using Ang's own field research data, can also explain the developmental trajectory of "Forest Hill." The locality's early push for infrastructure development can be attributed to Party secretary Chen, described as "The Builder," who formulated a development strategy prioritizing infrastructure expansion and won approval for construction of a new regional railway

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<sup>425</sup> Ibid 2016: 108-109.

<sup>426</sup> See Chapter 5, "From Building to Preserving Markets," Ang 2016.

after lobbying the center for years.<sup>427</sup> The city's subsequent shift to emphasize capital and investment attraction was inseparable from the later efforts of ambitious new mayor and subsequent Party secretary Yang, described as "The Recruiter." Ang recounts: "Whipping the beehive campaign into turbo mode, he set a goal of attracting one hundred investment projects every year at each of the three stages of planning, negotiation, and execution."<sup>428</sup> The next mayor, Mayor Lin, continued these efforts while placing new emphasis on the concept of "quality" and "development" instead of merely economic growth. Ang emphasizes that Mayor Lin's first work report was "significant because it underlined a turning point: the need to pursue quantity and quality of growth at the same time."<sup>429</sup> In Ang's case study, both the transitions from one stage of development to the next and the specific priorities of particular developmental stages coincide identically with the leadership terms of top local officials. This suggests that political leadership at the organization level drives and shapes the co-evolution of markets and institutions; it does not occur spontaneously or without direction.

### ***Linking Organizational with Institutional Change***

How then does the organizational change wrought by political leadership at the micro-level influence institutional change at the macro-level? At least four mechanisms link organizational and institutional change in China's state-owned economy: 1.) political

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<sup>427</sup> Ibid: 173.

<sup>428</sup> The "beehive campaign" refers to local Chinese officials' innovative method of attracting capital and investments in which all of a locality's agencies, regardless of formal function, are mobilized to recruit investors using any means at their disposal. Ang 2016: 174.

<sup>429</sup> Ibid: 176.

promotion of organizational leaders to the center; 2.) the center's selection of an organization as a model; 3.) formal diffusion of organizational experiences through meetings and publications; and 4.) informal sharing of organizational experiences.<sup>430</sup>

These mechanisms create feedback loops among organizations through the circulation of personnel and information. Organization heads who are promoted can exercise influence in new organizational settings based on their previous organizational experiences. Formal diffusion and informal sharing of organizational experiences of reform may promote emulation and learning as organization heads interact with other organizations and their leaders and/or study their experiences. These feedback loops function to maintain institutions if the organizational structures and strategies enacted or shared are consonant with existing institutions. Conversely, if they differ from existing institutions, then these flows of personnel and information act to gradually alter existing institutions.

Political leadership drives the operation of these mechanisms and feedback loops. As heads of organizations compete for promotion, they choose whether and how to maintain or modify the strategies and structures of the organizations they lead in response to both external factors (such as the institutional environment, the behavior of other organizations, or market competition) and internal factors (such as the situations of their own organizations or the political leadership of their predecessors). Political leadership is also an important factor generating the variation in organizational experiences that the state recognizes via political promotion of

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<sup>430</sup> These mechanisms are discussed separately here for the sake of clarity; however, they may overlap in practice. For example, the center may select an organization as a model, seek to formally diffuse its organizational experience of reform, and then promote its head to the center.

organization heads or model selection. It also shapes the extent to which organizations alter their structures and behavior by emulating and learning from a particular model. Political leadership is inseparable from the organizational experiences that constitute the raw material that the center formally disseminates through organized meetings and publications; in some cases the ideas and experiences of particular leaders are even their main focus.

The center serves important selection and bridging functions in these mechanisms and feedback loops. It serves a selection function by initiating and mediating flows of information and personnel. For example, the center decides which individuals are to be promoted or which organizations are to be recognized and put forward as models. The center also serves a bridging function—made possible by state agencies’ disparate capacity for control and influence over subordinate actors—by facilitating the flows of personnel and information among organizations at various levels of the administrative hierarchy. This is essential to overcome the multiple barriers to such exchanges taking place: geography, organization heads’ prioritization of other activities, their reluctance to share information or exchange personnel with potential competitors, and differences in administrative rank that differentiate the political activities and influence of organization heads.<sup>431</sup> However, the degree of state control and influence varies among the four mechanisms examined here. It is high for personnel promotion and model selection, medium for the sharing of organizational

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<sup>431</sup> Administrative rank confers important political privileges, including access to documents of varying grades of classification, invitations to meetings for officials of a certain rank, and the opportunity to participate in study groups and further training at the Central Party School of the Communist Party of China. Wendy Leutert, “Challenges Ahead in China’s Reform of State-owned Enterprises,” *Asia Policy* no. 21 (National Bureau of Asian Research, 2016): 87.

experiences through meetings, publications, and information reporting and low for the exchange of organizational experiences informally within industries and among peer groups. In the following sections, I outline the four mechanisms and illustrate them with empirical examples.

*Mechanism 1: Political Promotion of Organizational Leaders to the Center*

The first mechanism linking organizational with institutional change is the political promotion of organizational leaders to the center. These individuals may then reshape institutions through reform policy-making, designing and assessing national-level pilots, policy research, and public and private advocacy. While a large body of research has examined the political promotion of provincial and municipal leaders to central-level positions, scholars have paid less attention to the political mobility of officials in the state-owned economy.<sup>432</sup> Multiple possible aims motivate the promotion of state-owned enterprise heads to central-level positions. For example, state-owned enterprise heads may be appointed to regulatory or ministerial positions requiring specific industry or technical expertise in the sectors in which they worked previously. For those not yet approaching retirement age, appointment to the center may reflect the Central Organization Department's intention to broaden their

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<sup>432</sup> Zhiyue Bo, *Chinese Provincial Leaders: Economic Performance and Political Mobility Since 1949* (Armonk, NY: M.E. Sharpe, 2002); Zhiyue Bo, "Paths To the Top Leadership in China: The Case of Provincial Leaders," *Choosing China's Leaders*, eds., Chien-wen Kou and Xiaowei Zang (London: Routledge, 2013): 65-96; Eun Kyong Choi, "Patronage and Performance: Factors in the Political Mobility of Provincial Leaders in Post-Deng China," *The China Quarterly* 212 (2012): 965-981; Pierre F. Landry, Xiaobo Lü and Haiyan Duan, "Does Performance Matter? Evaluating Political Selection Along the Chinese Administrative Ladder," APSA 2014 Annual Meeting Paper, accessed on August 1, 2017 at: <http://ssrn.com/abstract=2452482>; Hongbin Li and Li-An Zhou, "Political Turnover and Economic Performance: The Incentive Role of Personnel Control in China," *Journal of Public Economics* 89 (2005): 1743-1762.

experience beyond state-owned industry as part of a grooming process for continued political advancement. For others, promotion to the center reflects recognition of lifetime career success and may be their final stop before retirement.<sup>433</sup>

The example of Chen Qingtai (陈清泰), former head of the Second Motor Vehicle Manufacturing Plant (第二汽车制造厂, *di er qiche zhizao chang*, hereafter referred to as Second Motor), shows how political promotion of organizational leaders can create broader institutional change. Mr. Chen, an automotive engineer by training, entered Second Motor in 1970 and rose through the ranks to serve as its chairman and general manager between 1984 and 1992. China's leaders originally planned Second Motor to be part of the defensive Third Front launched during the Mao era, establishing it in a remote and hilly area of Hubei province.<sup>434</sup> Subsequent efforts to develop locally autonomous production during the Cultural Revolution under the slogan of "large and complete, small and complete" (大而全, 小而全, *da er quan, xiao er quan*) left the Chinese automobile industry highly fragmented and dispersed. Second Motor, like other large state-owned industrial enterprises, faced the challenge of developing economies of scale and competitive advantage.<sup>435</sup> The center put

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<sup>433</sup> Wendy Leutert, "The Political Mobility of China's Central State-owned Enterprise Leaders," *The China Quarterly* (forthcoming).

<sup>434</sup> The Third Front was a massive infrastructure project that Mao Zedong launched in 1964 to industrialize central and western China in order to defend against the threat of attack or invasion by the Soviet Union or the United States. It included more than 1,000 projects and consumed more than 40% of China's capital construction budget between 1964 and 1980. Covell Meyskens, "Third Front Railroads and Industrial Modernity in Late Maoist China," *Twentieth-Century China* 40, no. 3 (2015): 238.

<sup>435</sup> William A. Byrd, "The Second Motor Vehicle Manufacturing Plant," *Chinese Industrial Firms under Reform*, ed., William A. Byrd (Washington D.C.: World Bank, 1992): 376, 408.



Second Motor directly under the central plan in 1984, thereby enhancing Mr. Chen's autonomy to exercise political leadership at the organization level.<sup>436</sup>

Second Motor sought to realize multiple central objectives under Mr. Chen's leadership. First, Second Motor needed to successfully implement the contract responsibility system, which the enterprise introduced in 1982.<sup>437</sup> However, Second Motor confronted serious development challenges because of its remote location and growing competition from more established industry competitors. To succeed, Second Motor needed to expand its production and product offerings by developing horizontal alliances with local producers within and beyond Hubei province. Second Motor also faced additional pressure to develop these horizontal alliances because the center viewed them as unofficial early experimentation in what it would ultimately formalize as state-owned enterprise groups with national-level pilots in 1991.

Mr. Chen's assumption of leadership in 1984 coincided with overheating of the national economy and the emergence of serious organizational problems after Second Motor's early implementation of the contract responsibility system.<sup>438</sup> He

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<sup>436</sup> This meant that the central State Planning Commission exercised administrative authority over Second Motor, not the local government. As Thun 2006 writes: "The result was the enviable position of having significant independence in decision-making ... and a great deal of leverage at the central level." Eric Thun, *Changing Lanes in China: Foreign Direct Investment, Local Governments, and Auto Sector Development* (New York: Cambridge University Press, 2006): 187.

<sup>437</sup> The contract responsibility system differed from the previous economic responsibility system reform because bureaus negotiated contracts with specific tax rates and profit-sharing arrangements with individual enterprises on a longer-term basis (typically three to five years) instead of every year. For Second Motor's contract details, see Byrd 1992: 387-388.

<sup>438</sup> While Second Motor continued to meet its contractual obligations, Mr. Chen describes how product quality began to deteriorate and overinvestment and even illegal sales occurred as subordinate production units prioritized expanding production and short-term material gain over product quality improvements and the company's long-term interests. 陈清泰 [Chen Qingtai]: 《一盘未下完的好棋》 [A Board of Good Pieces that Are Not Yet Entirely Played Out], 陈清泰 [Chen Qingtai]: 《汽车产业和汽车社会：一个汽车人的思考》 [The Automobile Industry and Automobile Society: Reflections of an Automobile Person] (Beijing: Zhongxin chubanshe, 2014). This part of the book is an excerpt

proposed a strategy of “shrinking the battle line” (缩短战线, *suoduan zhanxian*) to recentralize internal authority for decision-making and investment, and he initiated Second Motor’s gradual restructuring into a new three-level organizational structure.<sup>439</sup> Together, these moves enabled Second Motor to successfully implement the contract system while also simultaneously integrating an increasing number of local producers across a greater geographic area.<sup>440</sup> In addition, Mr. Chen announced that Second Motor must become a “operations and development company” (经营开发型企业, *jingying kaifaxing qiye*). This strategy comprised multiple elements: continual technological upgrading, development of new product offerings, and management training.<sup>441</sup> Mr. Chen described it as a broader effort to reorient Second Motor from being a producer in a planned economy in which the scale of production was first and foremost, to being a modern company in a market economy in which consumers’ demand for product variety and quality took precedence.<sup>442</sup> In addition to developing a new three-level organizational structure, Mr. Chen also altered Second Motor’s organizational structure in other ways. For example, he set up “three major centers”

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from a 7 hour oral history interview conducted by reporters from 《汽车商业评论》 [Auto Business Review] on September 27, 2011.

<sup>439</sup> The first level was the company headquarters, which would function as the center for company finances, strategy, and investment decision-making; the second level was the various divisions, like the procurement and sales departments, responsible for carrying out investment according to the plans of company headquarters and collecting profits and transmitting them up to headquarters; the third level was production units, responsible for production and quality and cost control in accordance with the plans of company headquarters. Chen 2011: 216.

<sup>440</sup> In 1981, Dongfeng Motors [Second Motor’s subsidiary corporation with which it would ultimately merge] integrated production by firms in eight provinces; by 1987 this number increased to 24 provinces. Byrd 1992: 410-411.

<sup>441</sup> For example, Mr. Chen invited European experts from the China Europe International Business School Training Center as well as Chinese economists including Wu Jinglian, Zhou Xiaochuan, Guo Shuqing, Luo Jiwei, and Jiang Yiwei to visit Second Motor and give trainings on topics such as stock shareholding system reforms. Chen 2011: 205.

<sup>442</sup> Ibid: 202.

(三大中心, *san da zhongxin*) at headquarters: the Technology Development Center, the Technical Equipment Center, and the Education Center.<sup>443</sup> He also led Second Motor to make a “three-direction leap” (三极跳, *san ji tiao*) by establishing new production and management centers in three locations at successively further distances from headquarters.<sup>444</sup>

Mr. Chen’s record of economic success at Second Motor prompted the Central Organization Department to promote him to the center in 1992 to serve as deputy director of the State Economic and Trade Commission under Zhu Rongji. Mr. Chen’s promotion put him in a position to influence the institutional evolution of state ownership through reform policy-making, designing and assessing national-level pilots, policy research, and public and private advocacy. For example, he played a key role in reform policymaking through his work preparing the pivotal Third Plenum report “Decision on the Establishment of Socialist Market Economy” in 1993.<sup>445</sup> As deputy director of the State Economic and Trade Commission, he moved from leading experimentation at the company level as the head of Second Motor to designing and assessing national-level pilots for enterprise reforms.<sup>446</sup> He strongly advocated shareholding system restructuring and the development of corporate governance, even during the mid-1990s when there was a conservative backlash against partial

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<sup>443</sup> Ibid: 212.

<sup>444</sup> These three locations were Xiangfan City in Hubei province, Wuhan in Hubei province, and Huizhou City in Guangdong province. Chen 2011: 212-213.

<sup>445</sup> During the preparation of this report, Mr. Chen was the head of the investigation group (调查组, *diaocha zu*), consisting of more than 100 people; his suggestions directly influenced the writing by the drafting group (起草组, *qicao zu*). Interview with drafting group member, Beijing, June 2016.

<sup>446</sup> For example, Mr. Chen led the State Economic and Trade Commission’s efforts to carry out the 1994 national-level experimental scheme on developing a modern enterprise system. The State Economic and Trade Commission was responsible for assessing 70 out of the 100 pilot enterprises; the State Commission for Economic System Restructuring was responsible for the remaining 30.

privatization of state-owned enterprises and the Chinese government had not yet equated the modern enterprise system with corporate governance.<sup>447</sup> In 1998, Mr. Chen became the Party secretary and vice-director of the Development Research Center of the State Council, where he assumed full ministerial rank and responsibility for policy research. Since then he has continued to advocate publicly and privately in support of market-oriented reforms, in particular corporate governance development and the need to transition from the state's management of assets to the state's management of capital.<sup>448</sup>

While Mr. Chen did not single-handedly redefine the institution of state ownership, the successful development that he led Second Motor to achieve prompted his promotion and enhanced his influence at the center to advocate for market-oriented enterprise reform policies. The experience of Second Motor under Mr. Chen's leadership showed how a single state-owned enterprise might pass through multiple organizational forms during the process of corporatization, thereby helping to legitimate the idea that state ownership could be embodied in multiple different organizational forms at the firm level. This idea enabled first the development of wholly state-owned industrial state-owned enterprise groups—which Second Motor spearheaded with its wide network of horizontal economic alliances—and then the partial privatization of large industrial state-owned enterprises through restructuring as

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<sup>447</sup> See Chapter 2 for detailed discussion of these two issues.

<sup>448</sup> 陈清泰 [Chen Qingtai]: 《董事长不是“一把手”》 [The Chairman is Not the “Number One Hand”], 《人民日报》 [People's Daily], January 10, 2000; 陈清泰 [Chen Qingtai]: 《深化国有资产管理体制改革的几个问题》 [Several Issues on Deepening the Reform of a State-owned Assets Management System], 《管理世界》 [Management World], 6 (2003): 1-4; 陈清泰 [Chen Qingtai], 《国有企业改革与公司治理》 [State-owned Enterprise Reform and Corporate Governance], 《南开管理评论》 [Nankai Management Review] 5 (2009): 4-5; 陈清泰 [Chen Qingtai] 《从管企业到管资本》 [From Managing Enterprises to Managing Capital] 《中国改革》 [China Reform] 1 (2014): 34-36.

shareholding companies and public listing—which Second Motor too pioneered as the first central state-owned enterprises to experiment with this reform.<sup>449</sup>

### *Mechanism 2: Selection of an Organization as a Model*

The second mechanism linking organizational with institutional change is the center's selection of a particular organization as a successful model for wide-scale emulation.

The Communist Party of China (CCP) has long employed models to influence individual and organizational behavior, by recognizing and elevating specific examples of success for broader emulation.<sup>450</sup> Models include individuals, like the mythologized worker Lei Feng, enterprises, like industrial pioneer Daqing Oil Field, and localities, like Dazhai village and Ganzhou city.<sup>451</sup> Models can influence institutional change in a particular direction by promoting the widespread adoption of particular forms of organizational structure and behavior, thereby narrowing the space for organizational leaders to formulate divergent strategies or to alter the structures of their organizations in alternative ways.

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<sup>449</sup> 陆一 [Lu Yi], 《谁开国企股份制先河?》 [Who Set the Precedent for Shareholding System Reform?], 《金融时报》 [Financial Times] (Chinese version), June 28, 2011.

<sup>450</sup> On the CCP's use of models throughout its history, see Sebastian Heilmann, "From Local Experiments to National Policy: The Origins of China's Distinctive Policy Process," *The China Journal* 59 (2008): 1-30; Sebastian Heilmann, "Policy Experimentation in China's Economic Rise," *Studies in Comparative International Development* 43, no. 1 (2008): 1-26.

<sup>451</sup> The CCP promoted Lei Feng as a famous model worker during the 1960s to mobilize Chinese citizens, especially youth. Daqing Oil Field in Heilongjiang province was a model enterprise for industrial development in the "learn from Daqing" campaign launched in 1964. Dazhai in Shanxi province served as the model village for agricultural collectivization in the "learn from Dazhai" campaign during the Mao era. Ganzhou in Jiangxi province is the model village for rural village modernization in the "new socialist countryside" campaign initiated by the Hu Jintao administration. Kristen E. Looney, "China's Campaign to Build a New Socialist Countryside: Village Modernization, Peasant Councils, and the Ganzhou Model of Rural Development," *The China Quarterly* 224 (2015): 909-932; Mitch Meisner, "Dazhai: The Mass Line in Practice," *Modern China* 4, no. 1 (1978): 27-62; Mei Zhang, "From Lei Feng to Zhang Haidi: Changing Images of Model Youth in the Post-Mao Reform Era," *Civic Discourse, Civil Society, and Chinese Communities*, eds., Randy Kluver and John H. Powers (Stamford, CT: Ablex Publishing Corporation, 1999): 111-123.

The example of state-owned enterprise Capital Iron and Steel Corporation (首都钢铁公司, *Shoudu gangtie gongsi*, hereafter referred to as Shougang) illustrates how political leadership and organizational change can ultimately influence institutional change through model designation. Founded in 1918 in the outskirts of Beijing, Shougang ultimately became one of the largest national steel companies in China and in the world.<sup>452</sup> The company reached the peak of its influence in 1992 when Deng Xiaoping publicly toured Shougang and it became the first enterprise in China permitted to open and own a national commercial bank.<sup>453</sup> The development of Shougang is inseparable from the political leadership of Zhou Guanwu (周冠五), who served as its Party secretary between 1959 and 1995 and its chairman between 1983 and 1995. Born in the same year as Shougang's founding, Mr. Zhou participated in the military resistance to Japanese occupation and the CCP's struggle for power during the Chinese Civil War. After the founding of the People's Republic of China in 1949, he joined the newly-established Shijingshan Iron and Steel Plant (石景山钢铁厂, *Shijingshan gangtie chang*—what would later become Shougang) in 1950 and worked there for nearly five decades until he retired in 1995. Mr. Zhou enjoyed personal ties and the trust of Deng Xiaoping, with whom he had fought during the Chinese Civil War, enhancing his existing autonomy for organizational-level experimentation.<sup>454</sup>

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<sup>452</sup> By 1993, Shougang had become the 18<sup>th</sup> largest steel producer in the world and the largest company in China by total profits. Peter Nolan: *Indigenous Large Firms in China's Economic Reform: The Case of Shougang Iron and Steel Corporation* (London: Contemporary China Institute, School of Oriental and African Studies, University of London, 1998): 20-21.

<sup>453</sup> Nicholas R. Lardy, *China's Unfinished Economic Revolution* (Washington D.C.: Brookings Institution Press, 1998): 67-69.

<sup>454</sup> While Mr. Zhou's close relationship with Deng Xiaoping prompted Shougang to be caught up in a backlash against Deng's reform policies during the late 1990s, including the arrest of Mr. Zhou's son Zhou Beifang on corruption charges in 1995, there is little evidence to suggest that he was a proxy of

Mr. Zhou's political leadership was decisive in Shougang's successful implementation of the contract responsibility system.<sup>455</sup> He led Shougang to sign its groundbreaking 15 year contract with the Beijing municipal government in 1982.<sup>456</sup> As Edward Steinfeld (1998) writes: "From the start, Zhou ensured that his name would become synonymous with Shougang and with the Shougang contract. He openly advocated this particular brand of reform in the years leading up to 1982 and, in a sense, staked his reputation and his career on its success."<sup>457</sup> During the implementation process, Mr. Zhou exercised political leadership by determining the specific strategies by which to increase the company's production output and profitability.<sup>458</sup> He emphasized that the contract responsibility system comprised both external relationships of responsibility—between the enterprise and the whole people (who formally owned state-owned enterprises)—and internal relationships of responsibility—among all the levels and areas inside the enterprise itself.<sup>459</sup>

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external political superiors at any time during his leadership tenure. For a rebuttal of suggestions that Shougang was "Deng's firm" and that Deng was a close patron of Zhou, see Edward S. Steinfeld, *Forging Reform in China: The Fate of State-owned Industry* (New York: Cambridge University Press, 1998): 190-193. On the end of the Zhou Guanwu era and backlash against Shougang in the mid-1990s, see John Hassard, Jackie Sheehan, and Jonathan Morris, "Enterprise Reform in Post-Deng China: Part A: The Fall of the Contract Responsibility System," *International Studies of Management & Organization* 29, no. 3 (1999): 65-68.

<sup>455</sup> Shougang's early experimentation with the economic responsibility system occurred between 1979 and 1981. During that time Shougang was a pilot enterprise for expanding enterprise autonomy reforms and it signed annual contracts with the Beijing municipal government.

<sup>456</sup> The contract required Shougang to increase the profits it remitted to the state by 6% every year from the baseline of the profits remitted in 1981 (the State Council increased this amount to 7.2% after the first year of the contract). Shougang was to spend 60% of retained profits on company development, 20% for collective welfare, and 20% for employee bonuses. It was required to assume full responsibility for maintaining and upgrading its assets. Nolan 1998: 26-27.

<sup>457</sup> Steinfeld 1998: 179.

<sup>458</sup> Here I discuss key examples of main strategies for Shougang's implementation of the contract responsibility system; this is not an exhaustive list.

<sup>459</sup> 周冠五 [Zhou Guanwu]: 《论承包制》 [On the Contract Responsibility System] and 周冠五 [Zhou Guanwu]: 《适应现代化大生产的需要, 加强思想作风教育, 建立企业内部承包制》 [Meeting the Needs of Large-Scale Modern Production], both published in 中共北京市委宣传部 [Beijing Municipal Party Committee Propaganda Department], 北京市思想政治工作研究会 [Beijing Political

Accordingly, he proposed a strategy of “contracting, guaranteeing, assessing” (包, 保, 核, *bao, bao, he*) involving comprehensive contracting down to the individual level; coordination among work units, departments, and positions; and strict assessment.<sup>460</sup> He called for implementing the contract responsibility system and modernizing management by managing every project according to five principles: completeness, standards, time limits, cooperation, and assessment.<sup>461</sup> Mr. Zhou also emphasized the integration of production and operations through “simultaneously grasping production, sales, distribution, and receipt” (产、销、运、收一把抓, *chan, xiao, yun, shou yi ba zhua*) in order to proactively coordinate and adjust Shougang’s operations in response to market factors, instead of the old system of taking orders from administrative superiors and reporting back up to them.<sup>462</sup> He also changed the company’s organizational structure. He cut the number of vice-managers at the top levels of management while simultaneously increasing the number of assistants.<sup>463</sup> He aggressively demoted or removed managers who failed to meet performance targets

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and Ideological Work Society], 首都钢铁公司 [Shougang Corporation]: 《首钢改革》 [Reform of Shougang], vol. 3 (Beijing: Beijing chubanshe, 1992).

<sup>460</sup> 周冠五 [Zhou Guanwu]: 《首钢改革十年》 [Shougang: Ten Years of Reform], in 首钢研究与开发公司 [Shougang Research and Development Company]: 《首钢承包制试点中的制度和政策》 [The Institutions and Policies of Shougang during Its Contract Responsibility System Experimentation] (Beijing: Guangming ribao chubanshe, 1989): 1-18.

<sup>461</sup> Shougang Research and Development Company 1989: 377.

<sup>462</sup> Mr. Zhou achieved this through employee organizing and communication initiatives such as introducing the “three discussions” (regular daily meetings at 8 o’clock, 1 o’clock and 5 o’clock) and publication of an internal newsletter, the 《情况通报》 [Circumstances Bulletin] to disseminate company matters. 冶金工业部 [Ministry of Metallurgical Industry], 中共首钢委员会 [Central Shougang Committee]: 《首钢实行经济责任制的经验》 [Shougang’s Experience Implementing the Economic Responsibility System] (Beijing: Beijing ribao chubanshe, 1982): 82, 344.

<sup>463</sup> Steinfeld 1998: 204.



across the firm.<sup>464</sup> These changes to the company's organizational structure were more than efforts to incentivize performance; they show a deliberate attempt to streamline management structure and thereby bolster the hierarchical exercise of authority.

Shougang achieved impressive improvements in performance during its implementation of the contract responsibility system. Profits increased by 20% per year on average between 1978 and 1985 and by 18% per year on average between 1985 and 1990.<sup>465</sup> While Mr. Zhou's political leadership was not the only reason for Shougang's successful implementation of the contract responsibility system, it was a critical factor.<sup>466</sup> As Peter Nolan (1998) concludes in his study about Shougang: "Analyses of Shougang have focused almost exclusively on the expanded autonomy given to Shougang as the explanation of its exceptional growth under the contract system. This monograph has argued that a relatively high degree of autonomy compared to other state enterprises is not a sufficient explanation. Many other enterprises adopted the 'Shougang system,' but few were as successful as Shougang. ... A distinctive feature of Shougang's growth was the central role for industrial entrepreneurship [of Zhou Guanwu]."<sup>467</sup> The Beijing municipal government

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<sup>464</sup> Between 1983-1984, more than 200 leading managers were removed from their posts. Between 1978 and 1990, 678 of Shougang workers at or above the level of plant and division management were demoted (643) or dismissed (35). Nolan 1998: 54.

<sup>465</sup> Beijing Municipal Party Committee Propaganda Department et al, vol. 2, 1992: 70, 90

<sup>466</sup> Other important factors in Shougang's success were high levels of employee mobilization and productivity, steadily increasing demand for steel in China's construction industry, and continued price controls on inputs and energy. One might also argue that the center selected firms with experienced management and strong performance for reform experimentation. However, this factor does not explain Shougang's particular success, because these conditions were also present for other pilot enterprises. Another factor that may have contributed to Shougang's successful implementation of the contract responsibility system was its earlier experience with operational autonomy during the Second Five-Year Plan (1958-1962), in which Shougang was responsible for budgeting, choosing equipment, and selecting suppliers. However, this experience, while important, was decades removed from the economic and political realities that Shougang and its leadership faced in the 1980s. See Nolan 1998: 26.

<sup>467</sup> Ibid: 75.

advanced a similar thesis in a 1982 report on the lessons of Shougang: “The Shougang experience is rich in content, comprehensive and detailed, with many things worthy of study. But the most fundamental experience remains the revolutionary spirit of fighting of the leadership, guiding the correct thinking, and adhering to taking improved economic efficiency as the center to lead production and the organization of production. If you do not study the Shougang experience from here, then you cannot grasp the important lessons of the Shougang experience, and you will not be able to truly learn the Shougang experience.”<sup>468</sup> And despite Mr. Zhou’s careful emphasis on workers’ contributions and democratic decision-making at Shougang, he too argued that leadership determined not only the success of an enterprise, but also the economic development of a country. In an internal lecture in 1987, Mr. Zhou stated: “If enterprise is not successful, not managed well, can the economy of a country improve? This is impossible. Therefore, getting enterprises to do well, especially large and medium state-owned enterprises, truly impacts the questions of the consolidation of socialist institutions and the rise and fall of nations....”<sup>469</sup>

Mr. Zhou’s success in pioneering the contract responsibility system at Shougang resulted in the emergence and official recognition of the “Shougang model” in 1982.<sup>470</sup> In that year, both Zhao Ziyang and Chen Yun praised the enterprise’s

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<sup>468</sup> Ministry of Metallurgical Industry and Central Shougang Committee 1982: 229.

<sup>469</sup> 周冠五 [Zhou Guanwu] 《工业企业的组织管理法——1987 年在首钢厂矿长培训班的讲课稿》 [Organization and Management of Industrial Enterprises—1987 Shougang Factory Head Training Class Lecture Notes] in Ministry of Metallurgical Industry and Central Shougang Committee 1982: 439.

<sup>470</sup> Feng Baoxing describes the Shougang model as comprising six elements: profit retention after meeting contract quotas; use of retained funds for development over consumption; linking the wage bill to annual profits; the right to market output; the long-term nature of its contract; and contracting involving all actors in the firm. 冯宝兴 [Feng Baoxing], 《论“首钢模式”》 [On the “Shougang Model”], 《经济纵横》 [Economic Review] 12 (1991): 47-51.

success.<sup>471</sup> Reformists and conservatives alike embraced Shougang's approach because it offered the prospect of improving enterprise performance and thereby stabilizing the government's fiscal revenues. Throughout the 1980s and into the 1990s, State Council leaders, the State Planning Commission, the State Economic Restructuring Commission, the Ministry of Metallurgical Industry, the National People's Congress, and the Beijing municipal government urged state-owned enterprises to "study the experience of Shougang and improve economic results" (学习首钢经验, 提高经济效应, *xuexi shougang jingyan, tigao jingji xiaoying*).<sup>472</sup>

Higher-level government authorities sent inspectors to Shougang and printed and disseminated booklets on Shougang's reform experience, as did Shougang itself. The Beijing city government sent government officials and heads of enterprises to Shougang to learn from its experience on site and also required work units to organize

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<sup>471</sup> Both Zhao Ziyang and Chen Yun endorsed Shougang but for different reasons. Zhao Ziyang's primary concern was the stabilization of fiscal revenues, whereas Chen Yun focused on the management of planning within enterprises. 赵紫阳 [Zhao Ziyang], 《首钢 1982 年进一步完善经济责任制的设想》 [Shougang 1982: Ideas on Further Improving the Economic Responsibility System]; 房维中 [Fang Weizhong], 《十三年纪事》 [Thirteen Years Chronicle] (Beijing: Zhongguo jihua chubanshe, 2013): 338.

<sup>472</sup> 《首钢的承包是成功的——全国人大部分常委、委员到首钢考察》 [Shougang's Contract Is Successful—Some National People's Congress Standing Committee Members and Members Inspect Shougang], June 1991; 《主人翁精神和科学技术相结合就能超过资本主义——国家计委各部门领导同志到首钢考察》 [The Combination of Master Spirit and Science and Technology Can Surpass Capitalism—Some Leading Comrades of Economic Planning Commission Inspect Shougang], June 1991; 《你们的成绩证明了工人阶级最有力量和智慧——国家体改委部分领导同志到首钢考察》 [Your Achievements Prove the Working Class Has Most Strength and Wisdom—Some Leading Comrades of State Economic Restructuring Commission Inspect Shougang], June 1991; 《一条迅速发展钢铁工业的新路子——冶金部部分领导同志到首钢考察》 [A New Path to the Rapid Development of the Steel Industry—Some Leading Colleagues of Ministry of Metallurgy Inspect Shougang], May 1991; 《希望首钢百尺竿头更进一步——北京市部分领导同志到首钢考察》 [Wishing that Shougang Advances Further—Some Leading Comrades of Beijing Municipal Government Inspect Shougang], May 1991; all published in Beijing Municipal Party Committee Propaganda Department et al, vol. 1, 1992: 173-179.

internal study groups on Shougang's experience.<sup>473</sup> Delegations from competitors like Anshan Steel and provinces as far away as Guangdong and Ningxia traveled to Shougang to study its successful experience.<sup>474</sup> The influence of the Shougang model reached its peak in 1992, when Deng Xiaoping toured the company on May 22. However, the shortcomings of the contract responsibility system were becoming increasingly evident: the problems of moral hazard and soft budget constraint persisted, state-owned enterprises' information asymmetry meant that many contracts ended up being highly favorable to enterprises, and there was no progress toward the development of a uniform tax system. In 1993, the Third Plenum quietly abandoned the contract responsibility system, and few would again mention the Shougang model as the example for state-owned enterprise reform.

Both the rise and fall of the Shougang model under Zhou Guanwu's leadership influenced the institutional evolution of state ownership. By making Shougang an official model, the center legitimated and affirmed the limited extension of authority for economic decision-making and resource allocation to enterprises and their leaders—together with responsibility for enterprise profits or losses. Shougang's success in delivering sustained economic gains during a multi-year contract period also provided political support for advocates of nationwide expansion of the contract

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<sup>473</sup> Ministry of Metallurgical Industry and Central Shougang Committee 1982: 227.

<sup>474</sup> 《首钢创造了具有普遍意义的经验——广东省考察团评论首钢》 [Shougang Created an Experience with Universal Meaning—Guangdong Province Investigation Delegation Assesses Shougang], January 1991; 《让首钢经验在内蒙古大地开花结果——内蒙古自治区考察团评论首钢》 [Let the Shougang Experience Greatly Flourish in Inner Mongolia—Inner Mongolia Autonomous Region Investigation Delegation Assesses Shougang], February 1991; 《首钢经验深刻丰富——鞍钢考察团评论首钢》 [The Shougang Experience is Profoundly Fruitful—Anshan Iron and Steel Corporation Assesses Shougang], March 1991; all published in Beijing Municipal Party Committee Propaganda Department et al, vol. 1, 1992: 180-183.

responsibility system.<sup>475</sup> With the formal abandonment of the contract responsibility system in 1993, Shougang's financial decline and ultimate collapse in 1995, and Mr. Zhou's forced retirement that year, the decline of the Shougang model also influenced institutional change in state ownership.<sup>476</sup> This was because the crux of the Shougang model that Zhou Guanwu pioneered was the idea that state-owned enterprises could succeed economically without privatization if the right incentives were in place. As Shougang and other state-owned enterprises began to struggle economically during the late 1990s, it prompted the Chinese leadership to consider partial privatization through share issuance as an alternative reform approach. The subsequent embrace of partial privatization would ultimately transform the institution of state ownership from the state's ownership of capital as well as assets.

*Mechanism 3: Formal Sharing of Organizational Experiences through Meetings and Publications*

The third mechanism linking organizational and institutional change is the formal exchange and diffusion of organizational experiences of reform through meetings and publications. The Chinese government employs a variety of methods to recognize, legitimate, discuss, and diffuse organizational experiences of reform. These methods include in-person meetings within organizations, such as study groups (学习班, *xuexiban*), using standardized content provided by administrative superiors and/or content created by organizations themselves. They also include in-person meetings

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<sup>475</sup> Prominent advocates of the contract responsibility system included CCP General Secretary Hu Yaobang, Vice-Premier Wan Li, Vice-Director of the State Economic Commission Yuan Baohua, and economist Li Yining.

<sup>476</sup> For a detailed account of Shougang's financial collapse, see Steinfeld 1998: 207-219.

across organizations, such as forums (座谈会, *zuotanhui*), in which an invited speaker or speaker shares his opinions and organizational experiences. Another type of such in-person gatherings includes discussion meetings (研讨会, *yantaohui*) or experience sharing meetings (经验交流会, *jingyan jiaoliuhui*) in which multiple participants discuss their views and organizational experiences. Formal exchanges across organizations can also occur on a more limited scale, for example through the exchange of visits (互访, *hu fang*) by individuals holding the same position across localities or in a particular industry to discuss the situations of their organizations. Finally, formal sharing of organizational experiences also occurs through the regular Party school trainings that Chinese officials are required to attend; these trainings too may include both Chinese and international participants.<sup>477</sup>

Government agencies also seek to formally share organizational experiences and political leadership approaches—of organizations tapped as key models for study as well as those simply considered successful—through publications.<sup>478</sup> They publish profiles of particular organizations' reform approaches and their results and distribute them to other enterprises, government bodies, and even the general public. The content of these publications varies in nature. It may be a record of a previous meeting, for example a compendium of reports and content originally presented at an earlier

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<sup>477</sup> For example, in 2013 the China Executive Leadership Academy Pudong (CELAP), a Party school in Shanghai, organized a week-long training session for 100 business leaders, including the heads of China's 53 core central state-owned enterprises, 15 Chinese financial sector representatives, 22 heads of private Chinese firms, and eight international representatives ranging from Deutsche Bank to Pepsi to Dow Chemicals and Proctor and Gamble. Interview with CELAP representative, Shanghai, July 2016.

<sup>478</sup> Government publications on organizational experiences range in length and focus, from simply a chapter in a longer work or a short feature in an internal journal, to entire works presenting multiple organizational case studies, to book-length treatments pairing profiles of single organizations and leaders with relevant laws and regulations.

discussion meeting (交流会文集, *jiaoliuhui wenji*). It may also be a profile drafted from materials shared by an organization and its leader and/or gathered through visits to the organization by an external inspection delegation (考察团, *kaochatuan*). In still other cases, government agencies feature the experiences of organizations and their leaders as parts of “how-to” publications like guidance manuals (指南手册, *zhinan shouce*). These publications use the experiences of specific organizations and their heads to show the steps to implement particular reforms set out in relevant laws and speeches by top leaders (which are often also included for reference).<sup>479</sup>

The government’s efforts to diffuse organizational experiences through meetings and publications may be followed by additional informational reporting or inspections. Through this informational reporting—which may be mandatory, encouraged, or optional—organizations and their leaders share feedback and evidence that they have at a minimum engaged with the content disseminated and at a maximum altered either the behavior or structure of their organizations as a result. In

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<sup>479</sup> Examples of such guidance manuals featuring company profiles include: State Economic and Trade Commission (Enterprise Reform Division), ed.: 《企业股份制改组运作指南》 [Enterprise Shareholding System Reform Operational Guidance Manual] (Beijing: Falü chubanshe, 2000); State Economic Restructuring Commission (Production System Division), ed.: 《企业股份制改造与资产重组方案》 [Enterprise Shareholding System Reform and Asset Restructuring Plans] (Beijing: Zhongguo shangye chubanshe, 1997); State Economic and Trade Commission (Enterprise Division): 《建立现代企业制度试点工作手册》 [Establishing a Modern Enterprise System Pilot Work Handbook] (Beijing: Zhongguo jingji chubanshe, 1996). The State Economic and Trade Commission also published specific guidance manuals on particular enterprises, like Xuji Corporation [许继集团] in Henan province and Yaxing Corporation [亚星集团] in Shandong province, as successful examples of state-owned enterprise reform and disseminated them to local economic and trade commissions. These works include speeches, interviews, and reports by their heads—Wang Jinian (王纪年) and Chen Hualin (陈华森), respectively—about the two enterprises’ strategies and organizational structure. State Economic and Trade Commission (Enterprise Reform Division), ed.: 《机制创新与三项制度改革：许继经验指导手册》 [Mechanism Innovation and Three Institutional Reforms: Xuji Experience Guidance Manual] (Beijing: Zhongguo jingji chubanshe, 2001); State Economic and Trade Commission (Enterprise Reform Division), ed.: 《企业物资采购管理暨推广亚星经验指导手册》 [Enterprise Materials Procurement Management: Promoting the Yaxing Experience – Guidance Manual] (Beijing: State Economic and Trade Commission, 1999).

some cases, administrative superiors may require organizations to formally report (汇报, *huibao*) the percentage of their subordinate units or employees who have organized and/or attended study groups on a particular topic. In other cases, organizational leaders will proactively show evidence that they have paid attention to the content disseminated and/or made corresponding efforts within their own organizations. For example, a state-owned enterprise leader may send a delegation to inspect a model enterprise and then write up a short report summarizing its visit and impressions, or he may describe efforts to alter organizational behavior and structure corresponding to the model and its positive results.<sup>480</sup> Administrative superiors may also dispatch representatives to carry out follow-up inspections (考察, *kaocha*) to assess the progress of particular organizations and their leaders and to update the center's previous judgments about the desirability of a particular reform approach.

These flows of personnel and information create feedback loops that reinforce or modify existing institutions by affirming and amplifying the effect of particular organizational experiences. Regular information reporting and inspections drive a feedback loop between the center and subordinate organizations. This is an iterative process in which the center affirms or modifies institutional direction based on organizational experience. Flows of personnel and information through in-person exchanges and publications also generate a feedback loop among organizations. If the behavior and structure of an organization designated as a successful example is

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<sup>480</sup> For example, the State Economic and Trade Commission's guidance manual on the "Yaxing experience" includes reports by heads of other state-owned enterprises about their efforts studying Yaxing and the subsequent effects on their operations. See State Economic and Trade Commission 1999: 188-270.



consonant with that of other organizations and existing institutions, then other organization heads are likely to cite this example to justify their current organizational structure and behavior and broader institutional change is unlikely. Conversely, if the political leadership of a particular leader and the behavior and structure of his organization represent a new type of organizational structure or behavior that differs from other organization heads' current practice or what they had previously interpreted as permissible according to existing institutions, then they may seek to modify the structures and behavior of their own organizations as a result. Aggregative substantive change across organizations can ultimately generate broader institutional change. However, emulation and learning may also be limited or superficial, in which case significant change to current organizational behavior and structure or to existing institutions is unlikely.<sup>481</sup>

#### *Mechanism 4: Informal Sharing of Organizational Experiences*

The fourth and final mechanism linking organizational and institutional change is informal sharing of organizational experiences. This may occur among peer groups of organizational leaders as well as between heads of organizations and their administrative superiors. Informal sharing of organizational experiences typically occurs within peer groups of organizational leaders: those who serve in similar official positions both within and across industries and regions. Heads of organizations in the same industry or locality have the most opportunities to share organizational experiences informally, for example on the sidelines of industry association meetings

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<sup>481</sup> Emulation and learning may also have limited organizational and institutional impact if a model is designated for only a limited number of organizations to study or if it falls from favor after a short time.

or through locally-based personal networks. Chinese officials also have opportunities to get to know their peers in different industries and localities, for example through the experience discussion meetings and Party school trainings discussed above. Networks originally created for the purpose of exchanging information specific to a given industry, locality, or group of officials at particular times can come to serve an alternative purpose of broader, long-term informal information exchange.<sup>482</sup> In addition, informal sharing of organizational experiences does not just occur among Chinese officials serving in similar positions, it also occurs between Chinese officials and their international counterparts, whom they get to know through meetings in China or through international conferences and trainings. Finally, sharing of organizational experiences also occurs through informal communications between heads of organizations and their administrative superiors, for example between central state-owned enterprises and SASAC officials. Information shared through these informal channels also generates feedback loops, and it is especially valuable because information shared informally is likely to be more candid—including discussion of missteps and failures as well as successes.

Informal sharing of organizational experiences occurs in numerous forms. In-person methods through which heads of organizations share information informally range from exchanges on the sidelines of official meetings or Party school trainings to conversations with their counterparts or superiors over meals or at other social gatherings. Informal sharing of organizational experiences also takes place through

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<sup>482</sup> For example, Coleman 1988 describes how study circles of South Korean youth from the same hometown, church, or high school provided the unit of social organization for later radical student activism in universities. Networks created for one purpose may be appropriated for another once formed. Coleman 1988.

more indirect avenues such as telephone conversations (still a communications staple in Chinese officialdom), emails, and now even virtual chats through the Chinese social messaging platforms QQ and WeChat.<sup>483</sup>

## ***Conclusion***

In this chapter, I outlined a co-evolutionary approach to analyzing economic reform linking the micro-level organizational change fashioned by political leadership with macro-level institutional change. Co-evolutionary analysis has three core elements. The first element is the mutual interdependence—and ultimately mutual constitution—of institutions and organizations. The second element is dynamic linkages—flows of information and personnel—that generate potential for multi-directional influence among actors as well as feedback loops linking organizations with one another and with institutions. The third element is processes of experimentation, competition, and selection through which organizations and their leaders interact with one another—including with their administrative superiors in the central government—and in doing so either maintain or modify existing institutions.

Political leadership is integral to all three of these elements of co-evolutionary analysis. First, organizational leaders mediate the influence of institutions on organizations by exercising political leadership—choosing whether and how to maintain or to modify existing organizational strategies and structures—in response to

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<sup>483</sup> For example, some local officials in Gansu province and in the municipality of Chongqing are now using WeChat groups to exchange information and experiences. 中国新闻网 [China News Network] 《“微信问政”: 天水清水县乡镇领导干部微信工作群速写》 [“WeChat Governance”: Tianshui and Qingshui Counties Township Leading Officials WeChat Work Group Sketches], May 16, 2016; 李薇帆 [Li Weifan], 《重庆日报》 [Chongqing Daily], 《县领导微信群每天交流心得》 [County Officials Exchange Experiences Every Day in WeChat Group], June 7, 2014.

institutional pressures and incentives. At the same time, the organizational continuity or change wrought by their political leadership serves either to reinforce existing institutions or to generate institutional change. Second, political leadership plays a critical role in the dynamic linkages—flows of information and personnel—that provide the potential for multi-directional influence and can generate feedback loops. Organizational leaders determine the content, amount, and veracity of the information they share with other peers and superiors through formal and informal channels. They also decide whether and how to respond to and use the information they receive from others. Finally, political leadership is central to processes of experimentation, competition, and selection. Experimentation itself is in important part the exercise of political leadership. As organizational leaders compete with one another in both economic and political selection environments, political leadership is both a method of seeking to deliver performance gains and a means by which to differentiate oneself politically. The center's selection of “winners” and “losers” among individuals and organizations is based on organizational performance as well as how well organizational leaders distinguish themselves from their peers and predecessors.

Political leadership, this chapter has argued, is a critically important factor in co-evolutionary scholarship in political economy. Political leadership drives and mediates the co-evolution of organizations and institutions; co-evolution does not occur spontaneously or without direction. Heads of organizations mediate how institutional incentives and pressures influence the structure and behavior of their organizations through their exercise of political leadership. In addition, political leadership provides an explanation for why and how organizations act proactively in a

variety of different ways to affect change in other organizations and in institutions.

However, heads of organizations cannot act however they wish. External factors, such as the institutional environment and the behavior of other organizations, and internal factors, such as resource endowments and configurations of influence among intra-organizational actors, may constrain their exercise of political leadership.

## Chapter 6

### **Conclusion:**

#### **Political Leadership in the State-owned Economy and Beyond**

Analysis of China's economic reform often implicitly adopts top-down or bottom-up perspectives. A top-down perspective emphasizes the central leadership's choices about economic policies, institutions, organizational forms, and resource allocations, while a bottom-up perspective highlights local actors' on-the-ground adaptation to changing external conditions in a decentralized context. These two perspectives draw attention to different sets of actors: top national elites and intellectuals at the center versus local officials, enterprises, and non-governmental organizations. They also entail different assumptions about the nature of economic reform and how it actually occurs. A top-down perspective suggests that economic reform is an adaptive yet deliberate and controlled effort, in which the center guides subordinate actors to grope for particular stones to cross the river. In contrast, bottom-up perspectives contend that economic reform is an emergent process that results from attempts by disparate actors to swim across by any means possible.

The political leadership approach proposed in this study expands these perspectives in three main ways. First, it examines a different set of actors—the heads of public sector organizations—to underscore both the individual agency and the intra-organizational dynamics involved in economic reform. Hidden from scholarly view in closed and often complex organizational worlds, heads of public sector entities in China are part of the state bureaucracy charged with realizing the center's reform

goals, but they still possess bounded autonomy to determine how precisely to act—or not—within the limitations imposed by particular organizational and institutional settings. In the state-owned economy, for example, China’s leaders have sought throughout the reform era to retain state ownership of a select number of enterprises while transforming them from struggling bureaucratic entities into profitable and globally competitive corporations. I show that heads of central state-owned enterprises faced with the same broad central goals can shape the reform process by modifying organizational strategies and structures in divergent ways. The center may direct organization heads toward certain stones in the river, but these individuals must still make decisions about how to get there, whether to search for other stones instead along the way, or whether to swim somewhere else entirely.

Second, a political leadership approach advances a dynamic, multi-leveled account of economic reform. It begins by showing how individual organization heads can shape economic reform by making choices within constraints about the strategies and structures of the organizations they lead. This exercise of political leadership generates the potential for multi-directional influence. The center might attempt to initiate and control the operation of feedback loops through methods such as personnel appointment, design of experimental pilots, or selection of particular model units for widespread emulation. However, the center does not ultimately control the decisions that individual leaders make within particular organizations and which also shape how those organizations are structured and behave. The concepts of “directed improvisation” and “guarded improvisation” aptly capture the dynamic nature of these interactions between center/local and state/non-state actors within vertical hierarchies

of influence.<sup>484</sup> A political leadership approach enriches these concepts by explicitly linking individual, organizational, and institutional levels of analysis.

Third, a political leadership approach addresses a missing factor in co-evolutionary analysis of economic reform. Beginning with the idea that institutions and organizations are mutually interdependent, it links the micro-level organizational change fashioned by individual leaders with macro-level institutional continuity and change. I identify four interrelated mechanisms through which political leadership and organizational change can generate institutional change in China's state-owned economy: political promotion of organizational leaders who redefine existing institutions; the center's selection of a particular organization as a model for wide-scale emulation; government-directed diffusion of successful experiences through means such as discussion meetings and publications; and informal sharing of successful and unsuccessful experiences between organizations and the center and among organizations themselves through information reporting and informal communications.<sup>485</sup>

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<sup>484</sup> Yuen Yuen Ang, *How China Escaped the Poverty Trap* (Ithaca, NY: Cornell University Press, 2016); Maria Repnikova, *Media Politics in China: Improvising Power under Authoritarianism* (Cambridge: Cambridge University Press, 2017).

<sup>485</sup> I illustrate the mechanism of political promotion with the case of Chen Qingtai's political leadership at Second Motor and his subsequent promotion to the State Council, where he subsequently shaped the institution of state ownership through policy-making, design and assessment of national-level pilot programs, policy research, and public and private advocacy for market-oriented reforms. For the mechanism of model selection, I discuss how the rise and fall of the "Shougang model" for implementation of the contract responsibility system under Zhou Guanwu's leadership influenced the institution of state ownership in two ways: 1.) by affirming early enterprise autonomy for economic decision-making and responsibility for enterprise profits or losses; 2.) by ultimately demonstrating that state-owned enterprises could not reverse their struggling performance just by changing firm-level incentives alone.



In this concluding chapter, I summarize the study's main findings, discuss its limitations and areas for future research, and outline its broader implications for analysis of China's politics and economy.

### *Summary of the Study*

In the introductory chapter, I present the study's two interrelated research questions. What explains change in organizations during the process of economic reform in China, both over time and across units? What factors explain changes in the institution of state ownership in China? I argue that political leadership is an under-theorized factor that can help to explain these interconnected processes of organizational and institutional change. I situate a political leadership approach relative to two broad competing perspectives on economic reform—the top-down, 'strategic design' and bottom-up, 'organic transformation' accounts described above—and describe how they fall short in answering these two questions. I introduce the types of leaders in the state-owned economy that the study examines and explain that I focus on economic reform in the state sector in China because its share of both the domestic and global economy is not only large but still growing.

Economic reform in China comprises not only the extension of decision-making authority away from the state toward markets but also the government-directed restructuring of state-owned assets. To assess variation in economic reform *across units* in China's state-owned economy, I therefore take the incidence of mergers among central state-owned enterprises as a key indicator. To evaluate economic reform *within units over time* in China's state-owned economy, I focus on

changes in levels of marketization in three areas: expansion efforts in international markets, shifts in influence among market-oriented and administrative entities within the firm, and how these entities conceptualize their relationship with international markets.

In Chapter 1, I outline a political leadership approach to studying economic reform. Specifically, organizational leaders in China's state-owned economy possess bounded autonomy to exercise political leadership by making choices about the specific strategies and structures of the organizations that they lead or those under their immediate administrative authority. This bounded autonomy originates from multiple institutional sources: the CCP's cadre management system, which functions as an instrument of macro-level rather than micro-level control; the decentralized context in which China's economic reform has occurred; and the increasing fragmentation of decision-making authority for policy-making and implementation among a growing number of actors. It also derives from organizational sources: the formal authority conferred by official leadership positions and long-standing governance and management practices stressing organizational hierarchy, authority, and conformity.

Chapter 2 steps back from the contemporary period to investigate how enterprise reform policies in China's state-owned economy since 1978 first created and then expanded space for the heads of state-owned enterprises and later the directors of SASAC to exercise political leadership. I argue that the center provided the initial "trigger" by granting state-owned enterprise heads greater autonomy through power delegation and profit-sharing reforms, but that ongoing devolution of

decision-making authority to enterprises and their heads has ultimately generated an increasingly dynamic and decentralized process of economic reform. I document this by summarizing key reform policies across four periods characterized by: a ‘dual track’ approach to economic reform (1978-1991); establishment of a socialist market economy (1992-1994); retrenchment of state ownership in the “commanding heights” (1995-2001); and internationalization and consolidation of the state sector (2002-present). Over the past four decades, state-owned enterprise heads’ space to exercise political leadership has expanded from the operational management of production to include greater control over the operational management of state-owned assets, and to an increasing extent also the operational management of state-owned capital.

In Chapter 3, I use a most-similar case study design to examine the effects of political leadership by consecutive chairmen of China Building Company, a central state-owned enterprise, on the firm’s economic reform over time. I conduct process tracing on a large body of qualitative and statistical data gathered during 15 months of participant observation at the firm’s headquarters in Beijing, one-on-one interviews with actors inside the firm, and secondary sources including company documents and yearbooks. I find that each of the two chairmen, Mr. Chen and Mr. Wu, exercised political leadership by formulating specific strategies to achieve the center’s broad goals and by changing organizational structure, and that this significantly altered the company’s global expansion efforts, shifts in influence among intra-firm entities, and how these entities conceptualized their relationship to international markets. The chapter concludes by evaluating this political leadership explanation for economic

reform relative to alternative explanations derived from top-down ‘strategic design’ and bottom-up ‘organic transformation’ perspectives.

In Chapter 4, I extend these findings to investigate the possible effects of political leadership on variation in economic reform across the central government’s entire portfolio of state-owned enterprises. Since 2003, SASAC-directed mergers have reduced the number of central state-owned enterprises under its administration from 189 to 101. However, the incidence of these mergers has varied across firms and over time. What factors affect the likelihood of central state-owned enterprise mergers? A top-level leadership hypothesis posits that state firms in industries assigned higher levels of strategic importance are more likely to experience mergers, as China’s leaders deliberately aim to concentrate state-owned assets in a small number of firms in the “commanding heights” of the economy. A middle-level political leadership hypothesis suggests that central state-owned enterprises are more likely to experience mergers when the SASAC director’s reform strategy emphasizes consolidation of state-owned assets.<sup>486</sup> Finally, a market competition hypothesis suggests that mergers should be most likely when competition in a particular industry is high, as only the fittest firms survive and the government acts to protect state firms’ market share and prevent price wars. Using logistic regression models to evaluate these hypotheses, I find strong support for the top-level leadership hypothesis and little support for the middle-level political leadership and market competition hypotheses. While these

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<sup>486</sup> While making central state-owned enterprises “large and strong” was the top priority for inaugural SASAC director Li Rongrong, his successor Wang Yong deprioritized this objective in a bid to make these firms “strong and excellent” through targeted company-level measures. The next director Zhang Yi articulated an amalgamated version of his predecessors’ strategies while prioritizing the immediate imperatives of fighting corruption and maintaining stability.

findings suggest an underlying political logic behind these mergers, they also point to the limits of a political leadership approach to economic reform, discussed in further detail below.

I proceed in Chapter 5 to examine how political leadership at the organization level can drive and mediate the coevolution of organizations and institutions, with a specific focus on Chinese state-owned enterprises and the institution of state ownership. Co-evolutionary analysis emphasizes three factors: mutual interdependence of organizations and institutions, dynamic linkages (flows of information and personnel), and processes of experimentation, competition, and selection. Political leadership is integral to all three. Organizational leaders choose whether and how to maintain or to modify existing organizational strategies and structures in response to institutional pressures and incentives, while the organizational continuity or change fashioned by their political leadership serves simultaneously to either reinforce existing institutions or to generate institutional change. They choose the content, amount, and veracity of the information they share with peers and superiors through formal and informal channels, while also deciding how to respond to and use the information they receive from others. Political leadership is also central to processes of experimentation, competition, and selection. Experimentation often involves choices about organizational strategy and structure, and the center's selection of "winners" among competing organizations and individuals is based on organizational performance as well as how organizational leaders distinguish themselves from their peers and predecessors through political leadership.

### *Areas for Future Research*

This study has focused primarily on organizational leaders' exercise of political leadership by making choices about organizational strategies and structures and its impact on economic reform. However, further investigation is needed to identify the tactics that organization heads use to carry out their leadership agendas against potential intra-organizational opposition—and how their subordinates respond. China Building Company's reform experience suggests that organization heads may draw from a wide repertoire of tactics, ranging from personnel ploys, emphasis on material and status gains, invocation of external threats, underscoring of administrative superiors' directives, and appeals to personal duty and morality. Additional study could seek to establish a common set of tactics across organizations, to address the conditions under which particular tactics are most likely to be effective, and to explore the range of possible responses and even counter-strategies by subordinate actors. This would engage both existing scholarship about the politics of the Chinese workplace during the reform era as well as studies of everyday resistance in other settings.<sup>487</sup>

Within state-owned enterprises, the politics of the relationship between the Party committee and top enterprise managers deserves further consideration. While the Party's role in enterprise governance has been a contested issue throughout the reform

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<sup>487</sup> Ching Kwan Lee, ed., *Working in China: Ethnographies of Labor and Workplace Transformation* (New York: Routledge, 2006); Ju Li, "Fight Silently: Everyday Resistance in Surviving State Owned Enterprises in Contemporary China," *Global Labour Journal* 3, no. 2 (2012): 194–216; Kun-Chin Lin, "Class Formation or Fragmentation? Allegiances and Divisions among Managers and Workers in State-Owned Enterprises" in *Laid-Off Workers in a Workers' State: Unemployment with Chinese Characteristics*, eds. Thomas B. Gold, William J. Hurst, Jaeyoun Won, and Qiang Li (New York: Palgrave MacMillan, 2009); James C. Scott, *Weapons of the Weak: Everyday Forms of Peasant Resistance* (New Haven, CT: Yale University Press, 2008).

era, the specific arrangements for Party governance vary by industry and enterprise and have changed over time. A starting point for analysis would be to examine the incidence of joint appointments in which enterprise heads serve simultaneously in top management and Party leadership roles.<sup>488</sup> While one might infer that holding joint Party and managerial appointments would augment an individual leader's authority within a particular organization, it could also signal efforts by administrative superiors to centralize their influence by simplifying the chain of command to a single person.<sup>489</sup> In cases where different individuals hold top Party and management roles, the potential for discord might be a possible constraint on organizational leaders' influence within the organizations they lead. In recent years, the prevalence of joint appointments for board chairmen and Party secretaries in central state-owned enterprises underscores the importance of closely studying the corporate governance arrangements in particular firms and their decision-making procedures. Analyzing the relationship between the Party committee and top enterprise managers reveals the tensions between Party control and enterprise autonomy that may impact individual leader's influence.

Such intra-organizational politics also need to be situated firmly within the context of an organization's own struggles for autonomy with its administrative

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<sup>488</sup> It is common for central state-owned enterprise executives to hold two of these positions simultaneously under the long-standing principle of “two-way entry, overlapping position holding” (双向进入，交叉任职, *shuangxiang jinru, jiaocha renzhi*). See State Council: 《关于选择一批国有大中型企业进行现代企业制度试点的方案（草案）》 [On Selecting a Group of State-owned Large- and Medium-size Enterprises to Implement Modern Enterprise Institution Pilots Program] (Draft)], November 1994.

<sup>489</sup> During the Hu Jintao period, the fact that the incidence of joint appointments was greatest in industries of high strategic importance—defense, electricity, and petroleum—lends support to the second interpretation. Wendy Leutert, “Challenges Ahead in China's Reform of State-owned Enterprises,” *Asia Policy* no. 21 (National Bureau of Asian Research, 2016): 95.

superiors. Before the establishment of SASAC in 2003, government bureaus or ministries exercised varying levels of influence over particular state-owned enterprises. Beyond the broad trend of devolution of economic authority away from the state toward enterprises since 1978, how might the political leadership exercised by the heads of various bureaus or ministries have influenced the autonomy that particular state firms enjoyed? Analysis of additional enterprise cases within and across industries would better illuminate the clashes and compromises from which state-owned enterprises and their heads gained or lost autonomy. Linking intra-enterprise and enterprise-bureau levels of analysis would also provide a fuller picture of the potential and limits for heads of different state-owned enterprises to shape the institution of state ownership through political leadership at the organization level.

Finally, investigation of industry-specific patterns in state-owned enterprise governance arrangements could also shed light on potential variation in organizational leaders' ability to shape organizational and institutional change. During the reform era, China's government has combined macro-liberalization with both selective re-regulation at the industry level and sustained efforts to develop a set of national champion firms at the enterprise level.<sup>490</sup> However, the prevalence of joint appointments for top managerial and Party positions in central state-owned enterprises operating in sectors of high strategic importance suggests the possibility that industry-specific patterns in enterprise-level governance arrangements may also exist, in addition to variation in regulatory policies toward particular industries. Such

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<sup>490</sup> Sarah Eaton, *The Advance of the State in Contemporary China: State-Market Relations in the Reform Era* (Cambridge: Cambridge University Press, 2015); Roselyn Hsueh, *China's Regulatory State: A New Strategy for Globalization* (Ithaca, NY: Cornell University Press, 2011).



examination of industry-specific enterprise governance practices within the state-owned economy could also build on existing research about sub-national variation in China's economic governance practices.<sup>491</sup> On the other hand, if industry-specific patterns in enterprise level governance arrangements are not evident, then this would suggest that the Party center and/or bureaus or ministries in particular industries have less ability to systematically constrain enterprise leaders' exercise of political leadership.

#### *Implications for Analysis of China's Politics and Economy*

A political leadership approach to the study of economic reform underscores the imperative of considering not only institutions but also the agency of organizational and individual actors. Top-down and bottom-up perspectives on China's economic reform both invoke institutions to explain continuity or change in organizational structure and behavior. A top-down perspective posits that the center's trial and error experimentation with various institutional arrangements alters how organizations are structured and act, while a bottom-up perspective suggests that institutions can emerge from below, as organizations adapt to changing external conditions, and become self-reinforcing. Despite their divergent views of institutional origins and change, both perspectives contend that institutions ultimately constrain organizational and individual actors in uniform and predictable ways. Yet narrowing the space for agency leaves these perspectives ill-equipped to explain the wide potential variation in policy

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<sup>491</sup> Nis Grünberg, "The Party-state Order: Essays on China's Political Organization and Political Economic Institutions" (Ph.D. dissertation, Copenhagen Business School, 2017); Yeling Tan, "State Strategies under Global Rules: Chinese Industrial Policy in the WTO Era," (Ph.D. dissertation, Harvard University, 2017).

experimentation and implementation across similar units or over time during the process of economic reform—despite similar institutional conditions and resource endowments. In contrast, a political leadership approach enables studying economic reform as an open-ended process that can evolve in myriad and sometimes unpredictable ways.

Studying political leadership at the organization level also provides a way to bring agency back in to state-centered accounts of economic reform. The developmental state paradigm, for example, posits a concept of “state agency” centered on the activities of bureaucratic actors within the state (such as state planning bodies) and their relationships with social and business interests (such as private enterprises).<sup>492</sup> It assumes that a fixed set of interests—such as the desire for greater resources and autonomy—motivate these actors’ behavior. The regulatory state framework’s state-centered focus similarly leaves the “agents” of regulation underexplored. It contends that markets can be governed through the state’s establishment of rules for proper market behavior and the creation of professional, rational institutions to enforce them.<sup>493</sup> Yet without considering political leadership, both the developmental state and regulatory state paradigms offer at best incomplete

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<sup>492</sup> Alice H. Amsden, *Asia’s Next Giant: South Korea and Late Industrialization* (New York: Oxford University Press, 1992); Peter Evans, *Embedded Autonomy: States and Industrial Transformation* (Princeton, NJ: Princeton University Press, 1995); Chalmers Johnson, *MITI and the Japanese Miracle: The Growth of Industrial Policy: 1925-1975* (Palo Alto, CA: Stanford University Press, 1982); Robert Wade, *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization* (Princeton, NJ: Princeton University Press, 1990).

<sup>493</sup> For China-focused applications of the regulatory state framework, see: Hsueh 2011, Shaoguang Wang, “Regulating Death at Coalmines: Changing Mode of Governance in China,” *Journal of Contemporary China* 15, no. 46 (2006): 1-30; Dali L. Yang, *Remaking the Chinese Leviathan: Market Transition and the Politics of Governance in China* (Palo Alto, CA: Stanford University Press, 2004).

and at worst deterministic explanations of economic reform.<sup>494</sup> “Circumstances do not make choices”—nor do aggregate state actors such as state planning agencies or regulatory bodies. A political leadership approach can help to explain why the same planning agencies might change reform policies in a particular issue area when external conditions remain unaltered, or why companies in the same industry might implement a particular regulatory policy in divergent ways despite similar conditions.<sup>495</sup>

In summary, a political leadership approach offers new analytic leverage on two questions central to the study of economic reform. What factors explain variation in policy experimentation and implementation across units, such enterprises or localities? Why do the structure and behavior of particular organizations change over time? It zeroes in on the origins of organizational variation and change by highlighting the bounded autonomy of organization heads to shape these processes and by identifying the mechanisms through which they do so. However, this study has also shown that organization heads’ potential influence may vary significantly depending on administrative hierarchies and issue areas. For example, middle-level SASAC directors and central state-owned enterprise heads seem to have little influence on mergers. However, current reform policies focused on state capital management—granting central state-owned enterprises increased autonomy to make decisions about capital management within their firms—are steadily increasing space for

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<sup>494</sup> Wade 1990: 257.

<sup>495</sup> They suggest that variation in economic reform outcomes occurs primarily because of differences in resource endowments, state capacity, and bureaucratic politics. For example, Johnson 1982 states: “The particular mix of tools changes from one era to the next because of changes in what the economy needs and because of shifts in MITI’s power position in the government.” Johnson 1982: 29.

organizational leaders to shape the consolidation of assets within state-owned enterprise groups and to craft strategies for their expansion in domestic and global markets.<sup>496</sup>

As Yuen Yuen Ang (2016) observes, how inputs are deployed and manipulated in the process of economic development is just as important as their existence: “There is no doubt that inputs like capital and labor are necessary for growth, but to conclude that such factors on their own will produce an economic miracle is like believing that eggs, sugar, and flour will turn into cake if left overnight in a mixing bowl.”<sup>497</sup> By highlighting agency as a missing ingredient, Ang’s cake-baking metaphor raises a more fundamental question—who exactly is doing the baking and how? A political leadership approach opens up space to examine individual agency within the state and its impact on economic reform. To extend the culinary metaphor, it can thus help to explain whether existing recipes are followed or new ones made, how the baking process actually occurs, and the potential variety of cakes that can be produced—even with similar ingredients.

More broadly, this project urges researchers to go forth and investigate the intra-organizational politics of economic reform in China, from the central level down to the grassroots. It is easy to assume that a uniform set of interests motivates organizational leaders—greater autonomy, larger budgets, increased personnel allocations, and potential political promotion—without going further to examine the variation in what these individuals actually do and its potential effects on economic

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<sup>496</sup> 《国资委启动四项改革试点》 [SASAC Starts Four Reform Pilots], *Xinhua News*, July 14, 2014.

<sup>497</sup> Ang uses this metaphor to simultaneously critique the notion of standard “recipes” for development and to provide a vivid figurative juxtaposition of static and dynamic explanations for economic development. Ang 2016: 7.

reform. Infighting among top political elites or the emergence of participatory governance institutions at the local level might initially appear much more attractive research topics than the processes of “everyday experimentation” which play out in the often mundane daily life of public sector organizations. But studying political leadership at the organization level underscores that much of China’s economic reform process occurs not in violent clashes between petitioners and local government officials or clandestine contests between dueling political elites, but rather in the “elbow politics” between organization heads, their subordinates, and their administrative superiors. This appears especially true at the central level, where autonomy and influence are just as much the goals and currency of politics as control over tangible resources like money and land. The political leadership approach proposed in this study offers an entry point into the world of intra-organizational politics in China’s state-owned economy and beyond.

## Appendix A

### **Case Study Analysis: Research Design and Data**

In Chapter 3, I use a two-part research design to assess the potential effect of political leadership on economic reform at the company level. First, I employ the most-similar case study method to select the units of analysis.<sup>498</sup> One of the oldest techniques of qualitative research, the most-similar case study method involves analysis of two or more cases that are similar across a range of independent variables except for the independent variable of interest.<sup>499</sup> This research design generates high internal validity because it allows background conditions to be held constant and reduces the potential for unobserved variables to impact the outcomes of interest. Second, I use process tracing to analyze the units selected.<sup>500</sup> This involves investigating the potential links between the independent variable of interest and the dependent variable, while remaining attentive to the possible effects of other variables. Such a research design combining the most-similar case study method with process tracing is “doubly robust,” because it first conditions on some confounders during the process of case selection (the matching of most similar cases) and then further addresses potential

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<sup>498</sup> Jason Seawright and John Gerring, “Case Selection Techniques in Case Study Research: A Menu of Qualitative and Quantitative Options,” *Political Research Quarterly* 61, no. 2 (2008): 304-306.

<sup>499</sup> Examples of studies that use the most-similar case study method include Crowley 1994 and Lieberman 2003. On the method of paired comparison see also Tarrow 2010. Stephen Crowley, “Barriers to Collective Action: Steelworkers and Mutual Dependence in the Former Soviet Union,” *World Politics* 46, no. 04 (1994): 589-615; Evan S. Lieberman, *Race and Regionalism in the Politics of Taxation in Brazil and South Africa* (New York: Cambridge University Press, 2003); Sidney Tarrow, “The Strategy of Paired Comparison: Toward a Theory of Practice,” *Comparative Political Studies* 43, no. 2 (2010): 230-259.

<sup>500</sup> I define “process tracing” as “attempts to identify the intervening causal process—the causal chain and causal mechanism—between an independent variable (or variables) and the outcome of interest.” Alexander L. George and Andrew Bennett, *Case Studies and Theory Development in the Social Sciences* (Cambridge, MA: MIT Press, 2005): 207.

alternative causes (those not controlled for during the case selection) and remaining empirical variation among the cases through process tracing.<sup>501</sup>

The specific cases that this study analyzes are consecutive board chairmanships at a central state-owned enterprise. I define a “case” as: “a spatially bounded phenomenon ... observed at a single point in time or over some delimited period of time.”<sup>502</sup> Focusing on consecutive board chairmanships in a single company increases confidence that the cases examined are similar along a range of independent variables that might affect economic reform at the firm level, including: industry, company size, revenues, profitability, ownership structure, geographic location, participation in international markets, state-business relations in a particular domestic context, and firm nationality. Holding these background conditions constant strengthens the study’s ability to isolate the variable of interest—the political leadership that these individuals exercise—and its impact on outcomes of interest. Examining consecutive leadership terms in a single firm since 2011 also minimizes potential concern that reform might differ across firm contexts or over long periods of time.

I choose to study consecutive board chairmanships within China Building Company because it is representative of Chinese central state-owned enterprises both in the construction industry and overall, with regard to its size, revenues, profitability, and official designation of strategic industry importance. Among central state-owned enterprises in the construction industry in 2013, China Building Company ranked

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<sup>501</sup> Richard A. Nielsen, “Case Selection via Matching,” *Sociological Methods & Research* 45, no. 3 (2016): 574-575.

<sup>502</sup> John Gerring, “What Is a Case Study and What Is It Good For?,” *American Political Science Review* 98, no. 2 (2004): 342.

second in size of total assets; fifth in revenue; fifth in ratio of state capital preserved; and sixth in profits.<sup>503</sup> Its ratio of state capital preserved and profitability was closely equivalent to central state-owned enterprises as a whole: it posted profits of approximately 11 billion RMB, compared to the average of 13 billion RMB for the 97 central state-owned enterprises reporting. Its ratio of state capital preserved of 107% equaled the average for the 85 central state-owned enterprises reporting.<sup>504</sup> As a construction company, China Building Company operates in a semi-protected industry: in between “strategic” sectors in which the state maintains “absolute control” and “commercial” sectors where no explicit protections for state ownership are given. During the study’s timeframe, China Building Company did not experience any major changes in its size, performance, or official industry designation.

I analyzed the data collected during my fieldwork at China Building Company through process tracing. Specifically, I investigated the potential links between political leadership and the selected indicators of economic reform at the company level. At the same time, I remained attentive to other alternative factors that could be explaining observed variation in economic reform over time, such as changes in policy by administrative superiors, external interference in company affairs, or economic shocks. This process involved continual inferences about counterfactual states of the world and corresponding triangulation of data to substantiate these inferences.<sup>505</sup> My

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<sup>503</sup> I use SASAC’s official industry categorization to identify this group of firms. 2013 is the most recent year for which data is available. State-owned Assets Supervision and Administration Commission, 《中国国有资产监督管理年鉴》 [State-owned Assets Supervision and Management Yearbook] (Beijing: Zhongguo jingji chubanshe, 2014).

<sup>504</sup> Author’s calculations based on reported data. Ibid.

<sup>505</sup> For example, one counterfactual state of the world might be a situation in which changes in administrative superiors’ directives affected the economic reform outcomes that I was studying at the



long-term immersion at the company strengthened my ability to conduct process tracing effectively because it enabled me to collect both “measurement evidence” (that events in a particular process tracing chain actually happened) and “identifying evidence” (that rules out confounding variables and processes).<sup>506</sup>

During my fieldwork, which included interning at China Building Company’s offices in Beijing during three different time periods over 15 months between 2014 and 2016, I collected qualitative and statistical data in three ways: participant observation, semi-structured interviews, and secondary sources.<sup>507</sup> I performed a range of tasks within and beyond my department, ranging from market research, translation, development of company marketing materials, and personnel training.<sup>508</sup> While interning at the firm two days a week full-time, from 8:30 AM to 5:30 PM, I kept detailed daily logs recording observations of company activities and exchanges with employees as well as my own activities, questions, and reflections.<sup>509</sup> I also conducted multiple one-on-one semi-structured interviews with department and company leaders.<sup>510</sup> In addition, I supplemented this firsthand data with an extensive record of secondary sources including company notices and documents (such as newsletters and work reports), company yearbooks, and media reports.

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firm level. To assess this, I closely tracked State Council and SASAC policies regarding the management of state-owned assets and state-owned companies.

<sup>506</sup> Nielson 2016: 574.

<sup>507</sup> I joined the company as an unpaid intern and worked two days a week full-time from January to June 2014, from September 2014 to March 2015, and from April to June 2016.

<sup>508</sup> Examples of market research include memos on infrastructure projects named in particular countries’ national development plans, their electricity pricing schemes, and current political situations.

<sup>509</sup> I wrote these daily logs directly on my computer using the notepad function. I took handwritten notes during group meetings and one-on-one interviews and then typed them up afterward.

<sup>510</sup> Each interview began with a set of fixed questions, followed by a series of open-ended queries tailored to the interviewee’s background and expertise. All interviews followed the protocol approved by the Cornell Institutional Review Board, number: 1507005681.

This project is one of the first studies on Chinese central state-owned enterprises to employ data gathered through participant observation.<sup>511</sup> Participant observation has multiple advantages over other data collection methods for studying economic reform in China.<sup>512</sup> First, it can generate reliable data that is simply not available elsewhere. Beyond widespread scholarly concerns about scarce or unreliable data—particularly given the demonstrated manipulation of some official statistics—researchers have been unable to access numerous Communist Party of China (CCP), state, and other organizations involved in economic reform policy-making and implementation.<sup>513</sup> Data gathered through participant observation therefore provides essential context for analyses of policy experimentation and implementation, because it enables more accurate identification of internal decision-making participants and processes. Participant observation is especially well suited for analyses of

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<sup>511</sup> Battat 1986 conducted participant observation through work in management education involving several Chinese industrial enterprises between mid-1977 and the end of 1979. Zhang 2014 also gathered data through participant observation at two Chinese state-owned companies in the automobile industry; however, her fieldwork at each of the total of seven firms in her study was at most two months in duration due to the comparative nature of her research. Previous studies about Chinese state-owned companies at the firm level have collected data through a variety of means other than participant observation, including: émigré interviews conducted outside of China (Walder 1988, Whyte and Parish 1984); surveys administered indirectly to state firm managers (Child 1996); short-term observation of managers (Boisot and Liang 1992), and repeated interviews conducted with workers outside and even within state-owned companies (Steinfeld 1998). Joseph Y. Battat, *Management in Post-Mao China: An Insider's View* (Ann Arbor, MI: UMI Research Press, 1986); Max Boisot and Xing Guo Liang, "The Nature of Managerial Work in the Chinese Enterprise Reforms: A Study of Six Directors," *Organization Studies* 13, no. 2 (1992): 161-184; John Child, *Management in China during the Age of Reform* (Cambridge: Cambridge University Press, 1996); William L. Parish and Martin K. Whyte, *Urban Life in Contemporary China* (Chicago: University of Chicago Press, 1984); Edward S. Steinfeld, *Forging Reform in China: The Fate of State-owned Industry* (New York: Cambridge University Press, 1998); Andrew G. Walder, *Communist Neo-traditionalism: Work and Authority in Chinese Industry* (Berkeley, CA: University of California Press, 1988); Lu Zhang, *Inside China's Automobile Factories* (New York: Cambridge University Press, 2014).

<sup>512</sup> I define participant observation as a method in which "the researcher takes part in the daily activities, rituals, interactions, and events of a group of people as one of the means of learning the explicit and tacit aspects of their life routines and their culture." Kathleen M. DeWalt and Billie R. DeWalt, *Participant Observation: A Guide for Fieldworkers* (Lanham, MD: Rowman Altamira, 2011): 1.

<sup>513</sup> Jeremy L. Wallace, "Juking the Stats? Authoritarian Information Problems in China," *British Journal of Political Science* 46, no. 1 (2016): 11-29.

organizational design, behavior, and change, because it sheds light on the drivers, mechanisms, and constraints within which these processes occur in particular organizational and institutional environments. In addition, participant observation can reveal the shared norms that guide individual and organizational behavior, through recurrent interactions between the researcher and actors within the social setting of a given organization. This is extremely difficult to do through interview-based fieldwork, in which the researcher typically has a single, one-on-one and brief interaction with an individual, often outside of the organizational setting in which the interviewee actually operates.<sup>514</sup> Finally, participant observation enables improved construct validity, for instance how “reform” should be conceptualized and measured at the company level.

Several factors were critical to the success of my fieldwork at China Building Company. The first was my introduction to the company through personal contacts in 2012. I applied for an internship through the company’s human resources department in 2013 and began my fieldwork there in 2014. The second factor was a fieldwork strategy focused on long-term, iterative immersion. This permitted sustained accumulation of trust and understanding, while periodic removal from the research setting facilitated critical reflection. This enabled me to make more accurate inferences by improving my ability to consciously discern between informants’ first-order reports and notions of what was happening in the corporate setting and my second-order conceptions as a researcher of what was actually occurring.<sup>515</sup> Finally,

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<sup>514</sup> An interviewee’s choice to hold an interview outside of the organizational setting in which he or she works, for example at home or at public venues such as restaurants or cafes, is entirely understandable given the scrutiny that meeting with a researcher might attract, and must be respected.

<sup>515</sup> John Van Maanen, “The Fact of Fiction in Organizational Ethnography,” *Administrative Science Quarterly* 24 (1979): 539-550.

my fluency in Mandarin was essential to perform my work responsibilities and interact with employees, and in doing so to gain a deeper understanding of the social dimensions of the workplace and the temporality of everyday life there.<sup>516</sup> All communications and secondary sources cited in Chapter 3 are my translations from the original Chinese, unless otherwise indicated.

However, several factors limited my data collection during the fieldwork. First, I naturally had the most interaction with employees who also worked in the department and member company where I was based in Beijing. Fortuitously, this member company's office building became the headquarters for the entire enterprise group just one month after I began my fieldwork; this enabled me to interact regularly with employees of the holding company as well as other member companies when they visited headquarters. In addition, I attended internal training sessions and company meetings that brought employees across departments together, ate meals with colleagues outside of my department and member company, and traveled outside of Beijing to meet with employees working in other member companies. In the spring of 2016, I also gave three trainings on cross-cultural communication to employees of different member companies; I concluded these sessions with questionnaires to gather additional information about the experiences and views of employees in different parts of the company.<sup>517</sup> Second, I did not have full access to the company's internal

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<sup>516</sup> Jordan and Lambert 2009 define the "temporality of everyday life" as "experiencing the boredom as well as the drama of mundane work and everyday life firsthand." Brigitte Jordan and Monique Lambert, "Working in Corporate Jungles: Reflections on Ethnographic Praxis in Industry," *Ethnography and the Corporate Encounter*, ed., in Melissa Cefkin (New York: Berghahn Books, 2009): 16.

<sup>517</sup> These questionnaires were informal and anonymous. I could relate responses to particular member companies because I asked participants which member company they worked in; however, I did not ask for any information that would have enabled identification of particular individuals, such as position titles.

computer network, which included an intranet with information about specific employees and projects, because I was not a formal full-time employee. To address this issue, I participated actively in the semi-official online QQ chat groups for our department and communicated regularly with employees about their work through QQ as well as in person. Third, I did not collect any information that was marked as for internal reference (内部参考, *neibu cankao*) or that I considered proprietary or sensitive, such as statistics on salaries, project costs, performance evaluations, or other issues. I did this to respect company regulations and to protect my own position as a foreign scholar conducting research in a public sector organization.<sup>518</sup> Despite these limitations, this study contributes to existing scholarship on Chinese central state-owned enterprises as one of the first to employ data gathered through participant observation.

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<sup>518</sup> The Xi Jinping administration's launch of a nationwide anti-corruption campaign after coming to power in 2011 heightened the potential sensitivity of my presence because it increased scrutiny of central state-owned enterprises' internal operations.

## Appendix B

### **Mergers Among Central State-owned Enterprises (2003-2015)**

| <b>2003<br/>Rank</b> | <b>Company Name<br/>(English / Chinese)</b>                | <b>Merged</b> | <b>Company Name<br/>(English / Chinese)</b>               | <b>Year</b> |
|----------------------|--|---------------|---|-------------|
| 5                    | China Aviation Industry First Group Corp.<br>中国航空工业第一集团公司  | To create     | China Aviation Industry Corp.<br>中国航空工业集团公司               |             |
| 6                    | China Aviation Industry Second Group Corp.<br>中国航空工业第二集团公司 | To create     | China Aviation Industry Corp.<br>中国航空工业集团公司               | 2008        |
| 21                   | China Electric Power Investment Corp.<br>中国电力投资集团公司        | To create     | State Electric Power Investment Corp.<br>国家电力投资集团公司       | 2015        |
| 25                   | China Network Communications Corp.<br>中国网络通信集团公司           | Into          | China United Telecommunications Co., Ltd.<br>中国联合通信有限公司   | 2009        |
| 32                   | China Second Heavy Machinery Co.<br>中国第二重型机械集团公司           | Into          | China Machinery and Equipment (Group) Co.<br>中国机械装备(集团)公司 | 2013        |
| 39                   | China Ocean Shipping (Group) Corp.<br>中国远洋运输(集团)总公司        | To create     | China Ocean Shipping Group Ltd.<br>中国远洋海运集团有限公司           | 2015        |
| 40                   | China Shipping (Group) Corp.<br>中国海运(集团)总公司                | To create     | China Ocean Shipping Group Ltd.<br>中国远洋海运集团有限公司           | 2015        |
| 55                   | China High-tech Investment Group Corp.<br>中国高新投资集团公司       | Into          | National Development and Investment Corp.<br>国家开发投资公司     | 2010        |
| 57                   | China Grain and Oil Group Corp.<br>中谷粮油集团公司                | Into          | COFCO Import & Export (Group) Co., Ltd.<br>中粮进出口(集团)有限公司  | 2006        |
| 58                   | China Packaging Corp.<br>中国包装总公司                           | Into          | China Chengtong Holding Co.<br>中国诚通控股公司                   | 2010        |
| 59                   | China Imported Automobile Trade Center<br>中国进口汽车贸易中心       | Into          | China Machinery and Equipment (Group) Co.<br>中国机械装备(集团)公司 | 2004        |

|    |  |           |   |      |
|----|--|-----------|---|------|
| 60 | China Business Group Corp.<br>中商企业集团公司   | Into      | China Chengtong Holding Co.<br>中国诚通控股公司                           | 2011 |
| 61 | China Huafu Trade Development Corp.<br>中国华孚贸易发展集团公司                                      | Into      | COFCO Import & Export (Group) Co., Ltd.<br>中粮进出口(集团)有限公司          | 2014 |
| 63 | China Huaxing Group Co.<br>中国华星集团公司  | Into      | China National New Holdings Limited Liability Co.<br>中国国新控股有限责任公司 | 2011 |
| 65 | Coal Science Research Institute<br>煤炭科学研究总院  | To create | China Coal Science and Technology Group Co., Ltd.<br>中国煤炭科工集团有限公司 | 2008 |
| 69 | China Agricultural Mechanization Research Institute<br>中国农业机械化科学研究院                      | Into      | China Machinery and Equipment (Group) Co.<br>中国机械装备(集团)公司         | 2009 |
| 71 | China Metallurgical Construction Group Corp.<br>中国冶金建设集团公司                               | Into      | China Metals & Minerals Import & Export Corp.<br>中国五金矿产进出口总公司     | 2015 |
| 73 | Metallurgical Automation Research and Design Institute<br>冶金自动化研究设计院                     | Into      | Iron and Steel Research Institute<br>钢铁研究总院                       | 2006 |
| 74 | China Haohua Chemical Group Corp.<br>中国昊华化工集团总公司   | To create | China National Chemical Corp.<br>中国化工集团公司                         | 2004 |
| 76 | China Chemical Supply and Marketing (Group) Corp.<br>中国化工供销(集团)总公司                       | Into      | China National Offshore Oil Corp.<br>中国海洋石油总公司                    | 2007 |
| 77 | China Chemical Construction Corp.<br>中国化工建设总公司   | Into      | China National Offshore Oil Corp.<br>中国海洋石油总公司                    | 2006 |
| 78 | China Blue Star (Group) Corp.<br>中国蓝星(集团)总公司   | To create | China National Chemical Corp.<br>中国化工集团公司                         | 2004 |
| 80 | China Light Industry Foreign Economic and Technical Cooperation Corp.<br>中国轻工业对外经济技术合作公司 | Into      | China Light Industry Group Corp.<br>中国轻工集团公司                      | 2008 |
| 81 | China Light Industry Machinery Corp.<br>中国轻工业机械总公司                                       | Into      | China Building Materials Group<br>中国建筑材料集团公司                      | 2004 |
| 82 | China Arts & Crafts (Group) Co.<br>中国工艺美术(集团)公司  | To create | China Technology (Group) Co.<br>中国工艺(集团)公司                        | 2006 |

|     |  |           |   |      |
|-----|--|-----------|---|------|
| 85  | China Textile Materials (Group) Corp.<br>中国纺织物资(集团)总公司                     | Into      | China Hengtian Group<br>中国恒天集团公司                                  | 2005 |
| 87  | China Textile Science Research Institute<br>中国纺织科学研究院                      | Into      | China General Technology Group<br>中国通用技术集团                        | 2009 |
| 90  | China Building Materials Science Research Institute<br>中国建筑材料科学研究院         | Into      | China Building Materials Group<br>中国建筑材料集团公司                      | 2004 |
| 95  | China Far East International Trade Corp.<br>中国远东国际贸易总公司                    | Into      | China Electronic Technology Group Corp.<br>中国电子科技集团公司             | 2009 |
| 96  | China International Enterprise Cooperation Corp.<br>中国国际企业合作公司             | Into      | China Chengtong Holding Co.<br>中国诚通控股公司                           | 2008 |
| 98  | China Geological Engineering Corp.<br>中国地质工程集团公司                           | Into      | China New Age Holdings (Group) Co.<br>中国新时代控股(集团)公司               | 2006 |
| 99  | China Four-Dimensional Mapping Technology Corp.<br>中国四维测绘技术总公司             | Into      | China Satellite Communications Corp.<br>中国卫星通信集团公司                | 2003 |
| 100 | China Real Estate Development Corp.<br>中国房地产开发集团公司                         | Into      | China Communications Construction Group Co., Ltd.<br>中国交通建设集团有限公司 | 2010 |
| 102 | China North Locomotive & Rolling Stock Industry Corp.<br>中国北方机车车辆工业集团公司    | To create | China Automobile Co., Ltd.<br>中国中车股份有限公司                          | 2014 |
| 103 | China Southern Locomotive & Rolling Stock Industry Corp.<br>中国南方机车车辆工业集团公司 | To create | China Automobile Co., Ltd.<br>中国中车股份有限公司                          | 2014 |
| 107 | China Harbor Construction (Group) Corp.<br>中国港湾建设(集团)总公司                   | To create | China Communications Construction Group Co., Ltd.<br>中国交通建设集团有限公司 | 2005 |
| 108 | China Road and Bridge (Group) Corp.<br>中国路桥(集团)总公司                         | To create | China Communications Construction Group Co., Ltd.<br>中国交通建设集团有限公司 | 2005 |
| 109 | China Foreign Cargo Terminal Co.<br>中国外轮理货总公司                              | Into      | China Ocean Shipping (Group) Corp.<br>中国远洋运输(集团)总公司               | 2005 |



|     |   |           |  |      |
|-----|---|-----------|--|------|
| 111 | China Post and Telecommunications Equipment Group Corp.<br>中国邮电器材集团公司             | Into      | China General Technology Group<br>中国通用技术集团                               | 2009 |
| 112 | China Great Wall Computer Group Corp.<br>中国长城计算机集团公司                              | Into      | China Electronic Information Industry Group Corp.<br>中国电子信息产业集团公司        | 2005 |
| 113 | China Satellite Communications Corp.<br>中国卫星通信集团公司                                | Into      | China Aerospace Science and Technology Corp.<br>中国航天科技集团公司               | 2009 |
| 115 | China Water Conservancy and Electric Power Co.<br>中国水利电力对外公司                      | Into      | China Water Investment Corp.<br>中国水利投资公司                                 | 2004 |
| 116 | China Water Investment Corp.<br>中国水利投资公司  | Into      | China Yangtze River Three Gorges Project Develop. Corp.<br>中国长江三峡工程开发总公司 | 2008 |
| 118 | China Agricultural Reclamation (Group) Corp.<br>中国农垦(集团)总公司                       | Into      | China Agricultural Develop. Corp.<br>中国农业发展集团总公司                         | 2009 |
| 119 | China Animal Husbandry and Commerce (Group) Corp.<br>中国牧工商(集团)总公司                 | To create | China Agricultural Develop. Corp.<br>中国农业发展集团总公司                         | 2004 |
| 120 | China Seed Group Corp.<br>中国种子集团公司  | Into      | China Sinochem Corp.<br>中国中化集团公司   | 2007 |
| 122 | China Arts and Crafts Import and Export Corp.<br>中国工艺品进出口总公司                      | To create | China Technology (Group) Co.<br>中国工艺(集团)公司                               | 2006 |
| 123 | China Foreign Trade Transportation (Group) Corp.<br>中国对外贸易运输(集团)总公司               | Into      | China Sinotrans Changhang Group Co., Ltd.<br>中国外运长航集团有限公司                | 2008 |
| 124 | China Native Produce and Animal Products Import and Export Corp.<br>中国土产畜产进出口总公司  | Into      | COFCO Import & Export (Group) Co., Ltd.<br>中粮进出口(集团)有限公司                 | 2004 |
| 126 | China Light Industry Products Import and Export Corp.<br>中国轻工业品进出口总公司             | Into      | China General Technology Group<br>中国通用技术集团                               | 2008 |
| 127 | China National Complete Plant Import and Export (Group) Corp.<br>中国成套设备进出口(集团)总公司 | Into      | National Develop. and Investment Corp.<br>国家开发投资公司                       | 2009 |

|     |   |           |  |      |
|-----|---|-----------|--|------|
| 129 | China Overseas Engineering Corp.<br>中国海外工程总公司   | Into      | China Railway Engineering Corp.<br>中国铁路工程总公司                         | 2003 |
| 130 | China Biological Products Corp.<br>中国生物制品总公司  | Into      | China Pharmaceutical Group Corp.<br>中国医药集团总公司                        | 2009 |
| 131 | China Medical and Health Equipment<br>Import and Export Corp.<br>中国医疗卫生器材进出口公司        | Into      | China Biotechnology Group Corp.<br>中国生物技术集团公司                        | 2005 |
| 132 | China Record Co.<br>中国唱片总公司   | Into      | China Chengtong Holding Co.<br>中国诚通控股公司                              | 2008 |
| 134 | China Fuma Forestry Machinery<br>Group Co., Ltd<br>中国福马林业机械集团有限公司                     | Into      | China Machinery and Equipment<br>(Group) Co.<br>中国机械装备(集团)公司         | 2007 |
| 137 | China Duty Free (Group) Corp.<br>中国免税品(集团)总公司   | Into      | China Travel Service Group Ltd.<br>中国国旅集团有限公司                        | 2003 |
| 138 | China Tourism Business Service<br>Corp.<br>中国旅游商贸服务总公司                                | Into      | China Travel Service (Group) Co.<br>中国中旅(集团)公司                       | 2004 |
| 140 | China Emerging (Group) Corp.<br>中国新兴(集团)总公司   | Into      | China General Technology Group<br>中国通用技术集团                           | 2009 |
| 142 | China New Age Holdings (Group) Co.<br>中国新时代控股(集团)公司                                   | Into      | China Energy Conservation<br>Investment Corp.<br>中国节能投资公司            | 2010 |
| 143 | Zhuhai Zhenrong Co.<br>珠海振戎公司   | Into      | South Light (Group) Co., Ltd.<br>南光(集团)有限公司                          | 2015 |
| 144 | China Ocean Aviation Group Corp.<br>中国海洋航空集团公司  | Into      | China Machinery and Equipment<br>(Group) Co.<br>中国机械装备(集团)公司         | 2007 |
| 146 | China Electronic Engineering Design<br>Institute<br>中国电子工程设计院                         | Into      | National Develop. and Investment<br>Corp.<br>国家开发投资公司                | 2009 |
| 147 | China Huanqiu Engineering Co.<br>中国寰球工程公司   | Into      | China National Petroleum Corp.<br>中国石油天然气集团公司                        | 2005 |
| 148 | China Coal International Engineering<br>Design and Research Institute<br>中煤国际工程设计研究总院 | To create | China Coal Science and Technology<br>Group Co., Ltd.<br>中国煤炭科工集团有限公司 | 2008 |
| 149 | China Haicheng International<br>Engineering Investment General                        | Into      | China Light Industry Group Corp.<br>中国轻工集团公司                         | 2008 |

|     |  |           |   |      |
|-----|--|-----------|---|------|
|     | Hospital<br>中国海诚国际工程投资总院   |           |   |      |
| 150 | China Textile Industry Design Institute<br>中国纺织工业设计院                       | Into      | China National Petroleum Corp.<br>中国石油天然气集团公司                     | 2007 |
| 151 | China Nonferrous Engineering Design and Research Institute<br>中国有色工程设计研究总院 | Into      | China Metallurgical Construction Group Corp.<br>中国冶金建设集团公司        | 2005 |
| 158 | China Electric Power Engineering Consulting Group Corp.<br>中国电力工程顾问集团公司    | To create | China Energy Construction Group Co., Ltd.<br>中国能源建设集团有限公司         | 2011 |
| 159 | China Hydropower Engineering Consulting Group Corp.<br>中国水电工程顾问集团公司        | To create | China Power Construction Group Co., Ltd.<br>中国电力建设集团有限公司          | 2011 |
| 160 | China Water Resources and Hydropower Construction Corp.<br>中国水利水电建设集团公司    | To create | China Power Construction Group Co., Ltd.<br>中国电力建设集团有限公司          | 2011 |
| 163 | China Printing Group Corp.<br>中国印刷集团公司                                     | Into      | China National New Holdings Limited Liability Co.<br>中国国新控股有限责任公司 | 2012 |
| 164 | Panzhihua Iron and Steel (Group) Co.<br>攀枝花钢铁(集团)公司                        | Into      | Anshan Iron and Steel Group Co.<br>鞍山钢铁集团公司                       | 2010 |
| 165 | Hanxing Metallurgical and Mining Administration Bureau<br>邯邢冶金矿山管理局        | Into      | China Metals & Minerals Import & Export Corp.<br>中国五金矿产进出口总公司     | 2004 |
| 166 | Luzhong Metallurgical Mining Group Co.<br>鲁中冶金矿业集团公司                       | Into      | China Metals & Minerals Import & Export Corp.<br>中国五金矿产进出口总公司     | 2009 |
| 167 | Changsha Institute of Mining and Metallurgy<br>长沙矿冶研究院                     | Into      | China Metals & Minerals Import & Export Corp.<br>中国五金矿产进出口总公司     | 2009 |
| 168 | China Luckai Film Group Co.<br>中国乐凯胶片集团公司                                  | Into      | China Aerospace Science and Technology Corp.<br>中国航天科技集团公司        | 2011 |
| 169 | Shenyang Chemical Industry Research Institute<br>沈阳化工研究院                   | Into      | China Sinochem Corp.<br>中国中化集团公司                                  | 2007 |
| 170 | China Huayuan Group Co., Ltd.<br>中国华源集团有限公司                                | Into      | China Resources (Group) Co., Ltd.<br>华润(集团)有限公司                   | 2006 |

|     |  |           |  |      |
|-----|--|-----------|--|------|
| 171 | Hualian Develop. Group Co., Ltd.<br>华联发展集团有限公司   | Into      | OCT Group Co.<br>华侨城集团公司   | 2005 |
| 173 | China Huandao (Group) Co.<br>中国寰岛(集团)公司  | Into      | China Chengtong Holding Co.<br>中国诚通控股公司                                | 2006 |
| 174 | China Yangtze River Shipping<br>(Group) Corp.<br>中国长江航运(集团)总公司                           | Into      | China Sinotrans Changhang Group<br>Co., Ltd.<br>中国外运长航集团有限公司           | 2008 |
| 176 | Shanghai Institute of Shipping and<br>Transportation Science<br>上海船舶运输科学研究所              | Into      | China Shipping (Group) Corp.<br>中国海运(集团)总公司                            | 2010 |
| 179 | Rainbow Group<br>彩虹集团公司  | Into      | China Electronic Information<br>Industry Group Corp.<br>中国电子信息产业集团公司   | 2013 |
| 181 | Shanghai Pharmaceutical Industry<br>Research Institute<br>上海医药工业研究院                      | Into      | China Pharmaceutical Group Corp.<br>中国医药集团总公司                          | 2010 |
| 184 | Tianjin Cement Industry Design and<br>Research Institute<br>天津水泥工业设计研究院                  | Into      | China Agricultural Mechanization<br>Research Institute<br>中国农业机械化科学研究院 | 2005 |
| 185 | China International Engineering<br>Consulting Design Institute<br>中机国际工程咨询设计总院           | Into      | China New Age Holdings (Group)<br>Co.<br>中国新时代控股(集团)公司                 | 2004 |
| 186 | China Post and Telecommunications<br>Advisory Design Institute<br>中讯邮电咨询设计院              | Into      | China United Telecommunications<br>Co., Ltd.<br>中国联合通信有限公司             | 2006 |
| 188 | China Gezhouba Group Co.<br>中国葛洲坝集团公司  | To create | China Energy Construction Group<br>Co., Ltd.<br>中国能源建设集团有限公司           | 2011 |
| 189 | Sanjiu Enterprise Group (Shenzhen<br>Southern Pharmaceutical Factory)<br>三九企业集团(深圳南方制药厂) | Into      | China Resources (Group) Co., Ltd.<br>华润(集团)有限公司                        | 2007 |
| *   | China Economic and Technical<br>Investment Guarantee Co., Ltd.<br>中国经济技术投资担保有限公司         | Into      | National Develop. and Investment<br>Corp.<br>国家开发投资公司                  | 2006 |
| *   | China Sinotrans Changhang Group<br>Co., Ltd.<br>中国外运长航集团有限公司                             | Into      | China Merchants Group Co., Ltd.<br>招商局集团有限公司                           | 2015 |
| *   | China National New Holdings Limited<br>Liability Co.                                     | To create | State Electric Power Investment<br>Corp.                               | 2015 |

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|---|---|------|---|------|
| * | 中国国新控股有限责任公司                                    | Into | 国家电力投资集团公司  | 2013 |
|   | China Grain Logistics Group Corp.<br>中国华粮物流集团公司 |      | COFCO Import & Export (Group)<br>Co., Ltd.<br>中粮进出口(集团)有限公司 |      |

*\* Indicates firms that were created or put under SASAC's management after publication of the original 2003 list.*

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